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INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

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SUBCOMMITTEE ON GENERAL SERVICES,
FEDERALISM, AND THE DISTRICT OF COLUMBIA

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GOVERNMENTAL AFFAIRS
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INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

THURSDAY, MAY 4, 1989

U.S. SENATE,
SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM,
AND THE DISTRICT OF COLUMBIA,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:06 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Jim Sasser, Chairman of the Subcommittee, presiding.

Members present: Senators Sasser, Lieberman, and Heinz.

OPENING STATEMENT OF SENATOR SASSER

Senator SASSER. The Subcommittee on General Services, Federalism, and the District of Columbia will come to order.

I want to say good morning to our distinguished witnesses this morning and good morning to all of our interested observers. I am pleased today to open this hearing, which is going to focus on our Nation's infrastructure problems. We are here to seek ideas on how Federal Government, State government, and local government can work together to find solutions to these very vexing problems we have with our infrastructure.

Now, the cost and difficulties of planning and building and maintaining this very complex infrastructure in the United States of America are not new. Much has been written in the public and private sector about these issues and various Congressional committees have held hearings on the topic of what is to be done about the problem of the infrastructure.

I think all of these reports lead us inescapably to one conclusion: our roads, our bridges, water and sewer systems, landfills, and the capital facilities of this United States of America of ours are wearing out faster than they are being repaired or replaced. We find that many of our bridges and roads that were built almost or over half a century ago are now wearing out on us or they need massive new repair.

The infrastructure in this country is simply aging and is not getting the attention that it needs, that it demands, and that the American people have a right to expect. The demand for new facilities is growing faster than our capacity to meet them.

So today, I am pleased to say that we shall hear from experts and knowledgeable representatives of Federal, State and local governments. Now, if these problems are to be properly analyzed and addressed, it must be done from the inner-governmental perspective.

If I may say a word about my native State of Tennessee—in Tennessee, we have been made acutely aware of the urgency of these infrastructure problems by two very tragic accidents—the collapse of a bridge on U.S. Highway 51 over the Hatchie River in western Tennessee, which left eight people dead, and the failure of a bridge on a local road over a railroad near Oliver Springs, Tennessee. This left, in its tragic aftermath, one dead teenager.

These accidents themselves, I think, reflect the inner-governmental nature of the system. One of the highway bridges that failed was maintained by State government. The other bridge that failed was maintained by local government. Both were subject to Federal bridge standards and both part of a State inspection program.

The facts are that all levels of Government share in providing for bridges. Both bridges that failed in Tennessee had been inspected. Both were scheduled for either replacement or for substantial repair. The Federal Highway Administration reports that 7,557 of Tennessee's 18,591 bridges are deficient in one way or another.

Now, Tennessee is not alone. The State of Tennessee represents what essentially is a microcosm in a glaring national problem. A report just published by the Congressional Research Service puts the national bridge deficiency rate at 41 percent—more than 41 percent of the bridges of the United States of America have a deficiency of one kind or another, of one magnitude or another.

Of that 41 percent, that means that 41 percent of the 577,700 bridges that were inventoried were deficient in one way or another. I do not think anyone underestimates the difficulty of making priority decisions about these infrastructure problems, but we have just got to realize that where the public safety of our people and the lives of our citizens are concerned, we have simply got to do a better job.

I have introduced legislation here in the Senate, Senate Bill 745, to set national standards and to ensure that the most dangerous bridges in this country get taken care of first. I am pleased to say that this bill is being sponsored in the House of Representatives by Congressman John Tanner. However, bridges are not the only infrastructure problem facing us here in the United States, although they have been getting the majority of the publicity.

The Federal, State and local governments have many other infrastructure problems. The inner-governmental aspects and responsibilities that define the problems with bridges are also reflected in our roads, in our water and sewer systems, and our mass transit systems, and the problem we have with solid waste disposal facilities.

No one knows better than I, as Chairman of the Budget Committee, the difficulty of trying to address the costly problems of the infrastructure in a time of severely-limited resources. Bringing down the deficit, of course, is critical to keeping interest rates under control. Keeping interest rates down is critical to allowing the State and local governments to float the tax exempt bonds that are necessary to meet many of these infrastructure problems.

But as we struggle to bring down our budget deficits, we have also got to remember that there is not going to be any balanced budget this year, next year, or any other year without a healthy and growing economy. Recent reports indicate that if we are going to have a strong economy, we have got to maintain a strong infrastructure.

Just let me share with our distinguished witnesses here today, and with my colleague Senator Lieberman, an interesting statistic. With regard to total spending for the infrastructure, it has been declining over the past few years. The Federal share of infrastructure spending for fixed capital formation declined from 41 percent in 1981 down to 34.5 percent in 1986.

It is estimated that to maintain the bridges of this country in a safe condition, the Federal Government needs to be expending a minimum of $3.5 billion a year. At the present time, and for a number of years, the Federal Government has been spending at a rate of about one-third of what is necessary to maintain safe bridges in this country.

Now, to the great credit of State and local governments across this country, and to the great credit of our own State government in Tennessee, these State and local governments have responded aggressively to the Federal retrenchment with new taxes and fees for infrastructure, and they have come up with their own creative financing and improved management to better address the infrastructure problems.

But we have got to do our share on the Federal level. This problem is simply too vast, too costly, too complex for the Federal establishment to walk away from it and say that this is the problem that addresses itself to the States, to the cities, to the counties. Certainly they have a role to play, but the Federal Government has a major role to play to see that we have safe bridges in this country, adequate highways, sewer and water systems that are up to the task, solid waste disposal facilities, and the list goes on and on.

Well, this morning I am pleased that the distinguished junior Senator from the State of Connecticut, Senator Lieberman, who has been at the forefront of these issues is here with us. Senator Lieberman is going to take a very active role in these proceedings and a very active role, I suspect, in legislation when it appears on the Floor.

I am sorry that I am going to have to leave these important hearings. We have the budget resolution on the Floor and I am managing that bill and it is up right now. So, I am going to leave this Committee in the very able hands of Senator Lieberman.

But before I leave, just let me say that we are particularly pleased today to have our distinguished colleague from the House of Representatives, Congressman Beryl Anthony, here with us today. Congressman Anthony has been making a great effort to probe the public finance issues central to the infrastructure discussion.

Congressman Anthony is a leader in this whole issue on a national basis, as well as being one of the leaders in the House of Representatives on this issue. I want to extend to you my thanks for appearing here this morning, Congressman Anthony, and my profound apologies for not being able to wait and hear your entire testimony, but I can assure you I will read it with interest in the record. I would now like to turn these hearings over to our very able colleague from Connecticut, Senator Lieberman. Thank you.

OPENING STATEMENT OF SENATOR LIEBERMAN

Senator **Lieberman** [presiding]. Thank you, Mr. Chairman, and as you leave me, I thank you for your leadership in calling this hearing, and also for the extraordinary job you have done in leading the Senate through the perilous course of adopting a budget resolution.

I thank also the staff that has worked so hard in preparing these hearings, and appreciate very much the witnesses who have traveled here today, and may I say, personally and particularly, the distinguished Treasurer of the State of Connecticut, my friend Frank Borges.

I have a prepared statement. I am going to ask that it be included in the record.

[The prepared statement of Senator Lieberman follows:]

Statement of Senator Joseph I. Lieberman

I commend Senator Sasser for convening this hearing on problems with our nation's infrastructure, and the subcommittee staff for their assistance in preparing for the hearing. I am looking forward to hearing from the witnesses who have generously offered their time and expertise to participate today, including the distinguished Treasurer from my home State, Frank Borges.

The subject of today's hearing is of great importance. Infrastructure is the economic lifeline of any developed country. A competitive economy cannot long survive without adequate transportation systems, water supply, and sewage and waste treatment. A crumbling infrastructure threatens both the economic health of the country and the physical health and safety of our people.

We have inherited the great infrastructure built by our predecessors—and railroads, highways, bridges, airports and city transit systems that move our people and fuel our industry, and the dams and water supply systems that serve our farms and our cities.

In recent years, however, we have let our infrastructure deteriorate. Our highways are in need of maintenance and repair, and bridges have collapsed in a number of states, including Connecticut. The Federal Highway Administration has found that 23% of the 575,600 bridges in the U.S. are structurally deficient. By 1993, up to half of the country's landfills are expected to be filled up. No major commercial airport has been built since the Dallas-Fort Worth airport in 1974. The National Council on Public Works Improvement has concluded that "the quality of America's infrastructure is barely adequate to fulfill current requirements, and insufficient to meet the demands of future economic growth and development."

Not surprisingly, the decline in our infrastructure has paralleled the decline in our investment in public works. Federal capital expenditures peaked in the late 1970's, and total public spending on infrastructure has dropped from 3.6% of the GNP in 1960 to 2.6% in 1985. Over the same period, our country has grown and the demands on our public infrastructure have dramatically increased.

This decline not only threatens the public health and safety, it threatens our ability to sustain continued economic growth and prosperity. Increased private investment and economic development had traditionally followed on the heels of public development of an enhanced infrastructure. The National Council's report notes, for example, that for every public dollar spent a year on our roads and bridges, the private sector spends $15 to use those improved facilities.

Moreover, productivity may be directly related to investment in infrastructure. Economist David Alan Aschauer recently reached this conclusion in a newsletter published by the Federal Reserve Bank of Chicago. Our rate of investment in public infrastructure capital has steadily declined, as has our rate of productivity. Our allies have fared much better. Japan, for example, has invested 5.1% of its output in public facilities from 1973–1985, achieving a growth in productivity of 3.3%. The United States, by contrast, has a public investment of 0.3% per year and productivity growth of 0.6% per year during the same period. Aschauer concludes that "a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, port facilities, airports and other facilities which aid in the production and distribution of goods and services."

Admirably, state and local governments have tried to pick up the slack, but the federal government has impeded their efforts. The 1986 tax reform legislation significantly hampered the ability of state and local governments to raise tax-exempt revenue for infrastructure investment, as some of the witnesses today will testify. We must be wary of allowing our short-term interest in raising federal revenue to blind us to the long-term costs of those methods. The long-term costs include reduction in economic growth and productivity. They also include interference with our environmental goals. Somehow, we must find a way to provide adequate landfills and sewage treatment facilities, or we will pay a heavy price in the future, and it cannot be done without adequate tax-exempt financing.

Hopefully, this hearing will increase public awareness of these problems and establish a record that will serve to encourage further investment in infrastructure at all levels of government.

Senator LIEBERMAN. Let me just briefly say—that perhaps it is not an accident that Senator Sasser have such a special interest in the problems of our infrastructure in America because we have both seen the most tragic results of problems with the infrastructure. Both of us have had bridges collapse. We had one collapse 6 years ago on I-95, which resulted in the death of three people.

The subject of today's hearing is of tremendous importance, if you think about the way we measure the growth and development of a new country, of a developing country. One of the ways we measure it is by the health of its infrastructure. We are obviously an extremely developed country and I think one of the things that has happened is that we have taken for granted the fact that our infrastructure determines the quality of our lives.

We were lucky to inherit an extraordinary infrastructure from the generations that went before us—our highways and bridges and railroads and airports and city transit systems that move and fuel our people and industry, the dams and water supply systems that serve our farms as well as our cities. But, as Chairman Sasser said so well, we have let that system deteriorate.

The National Council on Public Works Improvement concluded, "The quality of America's infrastructure is barely adequate to fulfill current requirements and insufficient to meet the demands of future economic growth and development." This decline not only threatens public safety. It also threatens our ability to sustain a healthy and prosperous economy.

The National Council pointed out that for every dollar spent per year on roads and bridges, private sector investment amounts to $15.00 to use those improved facilities. One interesting study recently showed that productivity may be directly related to investment in infrastructure.

As Chairman Sasser indicated, the Federal Government has stepped back, regrettably, from the field and admirably, State and local governments have tried to pick up the slack. But here too, unfortunately, the Federal Government has impeded their efforts. As so many of the witnesses know, and will testify to, the 1986 tax reform legislation significantly hampered the ability of State and local governments to raise tax exempt revenue for infrastructure investment.

We must be wary of allowing our short-term interest in raising Federal revenue to blind us to the long-term costs of those methods. The long-term costs include reduction in economic growth and productivity. They also include interference with some of our other societal goals, such as cleaning up our environment, because we are not really going to find a way to provide adequate landfills or sewage treatment facilities without adequate tax exempt financing.

I hope that these hearings and proceedings this morning will help to raise public and Congressional awareness of these problems, and establish a record that will serve to encourage further investment in infrastructure at all levels of Government.

I note the presence here of Senator Heinz of Pennsylvania and I would ask him now if he wishes to make an opening statement.

OPENING STATEMENT OF SENATOR HEINZ

Senator Heinz. Senator Lieberman, thank you. I do have a somewhat brief opening statement. I do not want to slow Beryl Anthony down, but I think this is an important subject to discuss and an important hearing. I commend the Senator from Tennessee, Senator Sasser, and of course, Joe Lieberman, for providing this opportunity to examine the state of America's infrastructure.

It seems to me that the real issue is how we can best enable those at all three levels—Federal, State, and local—to ensure that our infrastructure will be physically fit and fiscally stable well into the 21st century. Of course, we all know we have a very tough challenge ahead because, as the Congressional Budget Office and the Joint Tax Committee have pointed out, by the year 2000, the funding gap for critical infrastructure projects in this country will be $250 to $500 billion.

That is a gap. At least a $25 billion annual shortfall in infrastructure investment each year for each of the next 10 years. According to the CBO, by the way, the Federal Government spent $26 billion on that kind of infrastructure investment in 1988. And for those who are looking to the Federal budget, particularly with our budget resolution still on the Floor, our budget deficit makes it, frankly, unrealistic that the Federal Government would double that level of Federal spending.

So, that means we are going to have to be smarter about our public investments and, as I want to demonstrate briefly in a minute, create incentives for States and localities to do more on their own by making them offers they will not refuse.

Given limited resources at all levels, one of the strategies I will be proposing specifically is an incentive system that would use Federal money as a reward for cities, States, and localities that do the most to help themselves. Reba, could you put that chart on the easel for me, please?

This is another unreadable chart for those who forgot their glasses.[1] I am getting to the point, Joe, where I can barely make out my own charts. [Laughter.]

It is reproduced from the Road Information Program. You have the States going down vertically on the left-hand side. You have the sources of money—Federal aid, motor fuel taxes and so forth, going across the top. The numbers are percentages of each State's highway funding sources. The percents, therefore, add up to 100 percent going across.

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[1] See p. 208.

What that chart demonstrates is that States generate their funds from a large variety of sources—Federal assistance being a very major one, but motor vehicle taxes, registration fees and others also contribute. If you can see the chart and if you were to take the time to analyze it, what you would see is that for 23 of the 50 States, more than one-third of their highway funding comes from Federal assistance.

For example, up near the top, according to that chart, Federal aid alone represents 46 percent of California's highway funding budget; 23 percent is motor vehicle taxes; the remainder comes from a variety of sources. Some would argue that, well, there is nothing wrong with that since Southern California's interstate freeway system represents the bulk of that 46 percent and therefore, they should have, given that match, a higher percent.

But other people who have actually been to Southern California and tried to get from point A to point B anytime during the working week, would think that California's so-called interstate system mainly benefits local communities, providing commuter links between Orange County and Los Angeles, for example.

By the way, having been out there on a few occasions, I am one of those who tend to agree with that observation, that Federal dollars designed to facilitate interstate commerce are, in fact, in the case of Southern California, funding what are in effect local transportation systems and I would ask why we cannot give local communities and States an incentive to pay a greater share of the infrastructure burden, if they are going to use Federal money for, if you will, originally unintended purposes.

For a State where the huge volume of drivers recently necessitated adding a seventh symbol to new license plates, I am astonished that California does not have a completely dedicated source of State highway funding. They apparently do not and clearly, they should be paying more themselves for highway work and Federal assistance ought to be tied to it.

So, Mr. Chairman, the incentive system I propose would replicate that in a bill I have introduced, S. 672, the Bridge Improvement Act of 1989, which designates more Federal assistance to States that help themselves. Strangely enough, one of them is a State like Pennsylvania, my own State, that is committing substantial non-Federal funds to bridge work.

But the common denominator is that this approach requires the U.S. Department of Transportation here in Washington to determine how much each State is spending of its own resources—and that is the key—for, in the case of the bill I just mentioned, bridge work, and in the case of other modes, highways—to determine the rate at which each State is reducing its deficient, in the former case, bridge inventory.

Those States doing a good job on both counts would receive additional Federal funding. I hope that witnesses will respond to the concept, as well as to my specific proposal for such an incentive system, for all infrastructure investments. I know that I would be more interested in investing in an enterprise whose managers have already indicated their commitment to self-improvement.

Since that is really what I think we are going to be asked to do, come up with a little more Federal money, I think those of us who would like to be able to provide it would like to get something in return besides thanks.

Mr. Chairman, thank you.

Senator **Lieberman**. Thank you, Senator.

Now, I am delighted to welcome Congressman Beryl Anthony of Arkansas to these proceedings. I thank you, Congressman, for your patience as we made these opening statements. You have been a real point man in this whole issue and concern and we are delighted to have you here and look forward to your statement at this point.

TESTIMONY OF HON. BERYL F. ANTHONY, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARKANSAS [1]

Mr. **Anthony**. Thank you very much, Senator Lieberman and Senator Heinz. I thank Senator Sasser for coming in and opening the hearing today, and his kind remarks, inasmuch as we are neighboring States.

Senator Heinz, in terms of the legislation that you are introducing, I would take a quick look at comparisons of Arkansas and Pennsylvania and I say, if it is good for Pennsylvania, I have certainly got to believe that it is going to be good for Arkansas. Our numbers are fairly comparable with yours.

I would like to deviate for a moment from my printed statement to give you an update on State taxes. California is in the process of trying to raise additional revenues, and one of the stated purposes of those funds would be earmarked for roadways and mass transit systems. Arkansas is in the process of trying to raise additional revenues and part of it would be earmarked for highway repair. The Chairman's State of Connecticut is in the process of trying to raise additional State revenues and part of it would be used to pay for sewage plant repairs.

So, there is a continuation by the States to try to do something because they recognize that the Federal partnership has dissipated. I would like to add that as a supplement to my testimony.

Senator **Lieberman**. We will do that. Thank you, Congressman.

Mr. **Anthony**. Senator Sasser mentioned the recent death of 8 people in Tennessee on U.S. 51 and as a result, he has introduced S. 745 to focus the Senate's attention, and also the House of Representative's attention, on the necessary repair for bridges. In the Chairman's own State, on Interstate 95, certainly you are aware of the three people that were killed with a similar collapse of a bridge.

Just close at hand in the State of Maryland and on the East Coast, we are all constantly reminded on the nightly news of the sewer and garbage dispcsal systems and their failure because of sewage that has damaged the shellfish in the Chesapeake Bay and has washed up along the Atlantic coast.

These are just graphic and tragic examples of the crumbling of this Nation's infrastructure. They are tragic both in human terms and in economic terms. In my own home State of Arkansas, the results have only been evidenced in economic terms so far. A 1984 study of Arkansas cities and counties showed $862.9 million of critical repairs and replacement projects needed for streets, roads, drainage, bridges, and water, wastewater and solid waste disposal facilities.

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[1] See p. 47 for Congressman Anthony's prepared statement.

That is obviously one of the reasons that I became involved in the formation of the Anthony Commission, to try to focus some attention. But more importantly, to try to focus the legislative branch on what should be a public policy approach, rather than a grab to cure abuses in the tax code, sometimes for revenue sources because of the deficit. That has really been my bottom line, is to try to assimilate the information and the facts and redirect the national attention and public focus, and that is exactly what you are attempting to do through this public hearing.

A couple of success stories that I had in the State of Arkansas. The oldest bridge in the State of Arkansas is in my district. It is on U.S. Highway 82 and it crosses the Red River. It is in the process of being replaced because we did release money from the Highway Transportation Act. Unfortunately, as you well know, we had to do that over a Presidential veto.

I was able to also pass legislation that amended the bridge replacement legislation that would allow operating ferry boats. Believe it or not, we still have four in the State of Arkansas carrying huge volumes of traffic, two in my congressional district, both very dangerous. I am proud to say that both are in the process of being replaced with bridges as a result of that law being changed.

So, we are doing some good things. Senator Sasser mentioned tax exempt bonds. I would just like to again, deviate from my prepared text and tell you a story about the need to educate State and local officials in terms of where their focus should be.

I spoke to the National Association of Counties when they came to Washington, D.C.—thousands of them from all across the country. I had a little room that would hold approximately 200 people and my little sign outside said, "Tax Exempt Financing." I went in and I gave what I thought was a very exhilarating speech on a very dry subject. I had about 50 people there.

As soon as I finished, I walked out and started back to my office. I noticed right next door a sign that said, "Will the Garbage Trucks Roll?" Well, they had approximately 300 people, standing room, crowded out into the hall. And as I walked down the hall, I said, "Those people have their priorities out of shape." I said, "If we cannot get them the financing, the trucks will not roll."

So, part of what we are trying to do is redirect the public attention on the need for infrastructure with what has occurred. In terms of the Commission itself, having been a local prosecuting attorney for 10 years working with county officials, giving them some advice on bond counsel fees and proper projects and improper projects, I guess I got an early illustration of how tax exempt financing can help a local entity.

I came to Congress in 1979. I was fortunate to be placed on the Ways and Means Committee in 1981 by my colleagues. During the tax reform of 1986, I was a strong defender to try to fight back the elimination of tax exempt financing for State and local communities because I realized that Arkansas, and especially the people in the South and Southwest, had utilized that technique to a great extent for economic development and infrastructure replacement.

We had some successes in 1986, but unfortunately, due to some of the abuses that had been made public, there was a political climate that was difficult to save all of them.

Senator Lieberman, you might appreciate how I actually got involved in public finance. I got a call from Governor Clinton. He said we would love to throw a little appreciation party for you in Little Rock. Well, you know, politicians being vain, we love to have parties thrown for us and in our honor.

Well, I got to Little Rock, looked around, and I noticed that there were a lot of county judges there, there were a lot of State senators and State representatives. There were a lot of mayors there. I looked around and there were also some representatives from the bonding houses, as well as Wooten Epes, and I kind of had a feeling then that I had been hooked.

Governor Clinton got up and made some nice remarks about me, but then he said I'll assume that Congressman Anthony is going to be our savior and defender to not have tax exempt financing eliminated during tax reform. So, I realized there was a hook with praise.

But since then, I have been an outspoken supporter, and we hit on the idea of trying to get a broad-based, knowledgeable commission put together to study public finance from the public policy standpoint, because sometimes laws were changed for abuse reasons and some were changed for revenue. In some cases, people just absolutely, philosophically are opposed to tax exempt financing. We will just have to fight that battle when we propose legislation.

But the timetable for our Commission, after approximately 16 months of really dedicated, hard work, the report should be out within the next 45 days. We obviously would submit a copy of the report to you personally and if you would see fit to make it a part of the record, then that would be your decision, depending on what the length and the volume of it is.

But I think it will be a report that we can then take and hopefully devise some legislation. Senator Heinz has devised legislation. Sasser has devised legislation. I would love to devise legislation based on what the Commission finds.

I would like to spend the rest of my time to just highlight some of the important failures in this partnership between the Federal and the State and the local level, and some of the need to try to demonstrate why we should all work collectively to try to get something done.

First, when President Reagan took office, the public debt was $914 billion. It is now $2.3 trillion. The Senate has taken up the budget resolution. The House has taken up the budget resolution and that is about all we talk about. Can we afford anything? Well, let us take a look at the record.

In 1980, funding for the Environmental Protection Agency's wastewater construction grant program was $3.4 billion and it dropped to $1.2 billion in the 1990 budget. Yet, the EPA has estimated that 400 cities and towns will be unable to meet the deadline of cleaning up their secondary treatment facilities.

When we reauthorized the Clean Water Act, we provided only $2.46 billion for what EPA recently estimated will require $83.5 billion to construct the facilities to live by the standards that the Federal Government is forcing upon State and local governments.

On public transportation, the funding has been cut from $3.527 billion to $1.523 billion, while the transportation congestion increased dramatically, resulting in decreased productivity and competitiveness. The Federal Highway Administration says that over 60 percent of the United States' paved roads and 25 percent of the interstate highway system need resurfacing or reconstruction. And 35 percent of the interstate system will have outlived its design life by 1990, while 45 percent of the Nation's bridges are structurally deficient or obsolete.

In your opening statement, you mentioned about productivity. In September of 1988, a letter from the Chicago Federal Reserve Bank concludes that countries which produce high public investment in infrastructure have higher productivity growth, "Thus a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, ports, airports, and other facilities which aid in the production and distribution of goods and services."

Another number that I think we need to be aware of is that during the last 20 years, infrastructure spending in the United States, as compared with the Gross National Product, has dropped from 2.3 percent down to 1 percent. So, we have had our attention misdirected and I think we are going to have to redirect it.

New York City intends to spend $57.3 billion on infrastructure during the next decade, while New York/New Jersey Port Authority will spend over $5.8 billion during the next 5 years, and the Metropolitan Transportation Authority will spend about a billion dollars per year during the decade. New York City alone will need about $80 billion in required investment between now and the beginning of the 21st century.

Affordable housing—the direct Federal funding has been cut from $26.98 billion in fiscal year 1981 to $7.851 billion in fiscal year 1989, while tax incentives to provide housing for just about everyone but the affluent have been eliminated.

If you take all of the total—and I think this is the most devastating number, if you take all of the programs and if you look at them from 1980 through 1987, you will see that Federal aid to States and cities has declined 37 percent in real terms. That means that it has fallen to its lowest level since the 1960's.

Well, obviously then, the State and local governments have been required to pick up the additional costs because of the new federalism. I am not totally opposed to the new Federalism, and I think it is healthy, but I do not think that the Federal Government can mandate requirements and then walk away without any financial support or help.

My full statement will show emphatically—and I am sure other witnesses will hit on this—where State and local governments have increased their revenue intake and how many of them will be considering taxes in the immediate future. My study shows that of the 50 States, 42 have or are in the process of raising local revenues.

So, it is interesting, when a President gets elected with a slogan that says, "Read my Lips," that responsible Governors, responsible county judges, and responsible mayors are asked to pick up the slack because the Federal partnership has been dissipated. But the people are responding.

In my own State, over two-thirds of the counties have passed a sales tax and there is a success ratio in the 90th percentile. So, when the public knows that there is a specific need and reason, they will respond. It is just when you lay it out in some nebulous terms and you just say you want revenue for whatever purposes, that is when the public does not give you the support.

Senator LIEBERMAN. Congressman, when you say success ratio, what do you mean in this case?

Mr. ANTHONY. I mean we are talking about the voters going to the polls and pulling the lever—I am going to pay more taxes in my own community because I want better services rendered by my county judge and my mayor. I think that is astonishing. So, when the local community is willing to go to the public and say we need more taxes, maybe for wastewater treatment facilities, a hospital.

I had a hospital in Prescott that was in the process of closing down. The local people taxed themselves for 5 years specifically to keep the hospital open. That tax passed by about 85 percent to 15 percent. So, it can be done if you have progressive and alert leaders who are willing to go out there and do it.

My bottom line, Senator Lieberman, is, when you look at the record, the infrastructure has crumbled and is continuing to crumble. It leads to lack of competition and productivity. The Federal partnership has been shattered. I hope your hearing clearly demonstrates that it needs to be repaired, and I hope that we can take the legislative initiatives to give that help back from the Federal level.

My own area will be in the tax exempt financing area because I think that is a place where we can provide cheaper credit to State and local governments and we can give them some ability to determine, on their own, what are the most needed projects within their own States and within their own regions. What we just need to do is define what the public policy should be in terms of a tax expenditure that obviously costs the Federal Government some dollars.

My testimony is replete with other examples. It talks about some of the abuses, such as a little community in Illinois called Deerfield. It caused us a great deal of trouble. They went out and sold a lot of bonds, they put them in the bank, they drew more interest than they were paying, and they ended up financing their government as a result of the overcharge that they were able to earn. At the same time, it earned us a lot of amendments in the Ways and Means Committee to try to restrict tax exempt financing.

So, what we have got to do is strip out those types of abuses, but we have got to find a better way to make the system work so that the State and local governments can utilize tax exempt financing to repair the infrastructure.

I want to commend both Senator Sasser and yourself for conducting these hearings. They are extremely important. Sometimes, people think that roads, bridges, wastewater treatment facilities and landfills are boring because they are things we take for granted. But if we allow them to continue to deteriorate, then we will not be able to compete domestically, nor will we be able to compete internationally.

So, I think what you are doing really is the economic savior and backbone of any future hope of growth and development of the United States. I want to applaud you for your efforts and I hope your hearings are an outstanding success.

Senator LIEBERMAN. Thank you, Congressman, and thank you for taking the time to come over here and we would turn the applause to you. Our hope here again, is that we can raise the level of public awareness of the problem. I can assure you that the Chairman of the Subcommittee, Senator Sasser and I are serious about it and intend to hang in there and try to do something on it and we look forward to a very productive partnership with you in that effort. I appreciate your time. Thank you for coming over.

We would now call the first panel of witnesses from the State perspective and that is, I would ask both the Honorable Frank Borges, Treasurer of the State of Connecticut and the Honorable Howard Yerusalim, Secretary of the Department of Transportation of Pennsylvania to come forward.

If I may say, by way of procedure, to these two gentlemen and the other witnesses, we have copies of your testimony and I am now, by this act, indicating that the full text of your testimony will be included in the permanent record of this hearing. I ask you therefore, to please try to summarize, at the outset, your testimony, to 5 to 10 minutes.

Just to give you a sense of the management that we all are going to have to do here to have this be a good hearing, we have to recess at 12:30. There may be a vote or two that I have to go over to the Senate floor for, which will mean that we will have some breaking time. We have three real good panels here. So, I want to make sure that everybody who has come has an opportunity to testify and we have a chance for a little bit of an exchange as well.

Let me begin with some admitted pride and parochialism by calling on our great State Treasurer, Frank Borges, with whom it was my pleasure to work when I was Attorney General of Connecticut. He has been a real leader in infrastructure financing problems. Treasurer Borges, please proceed.

TESTIMONY OF FRANCISCO L. BORGES, TREASURER, STATE OF CONNECTICUT [1]

Mr. BORGES. Thank you, Senator Lieberman. Thank you very much for your very kind words. It is indeed a pleasure and honor to be here before you and this Committee. I am here today both as the Treasurer of the State of Connecticut, and as the representative of the National Association of State Treasurers. It is in that capacity that I appear before you to discuss the financial impact on the States of current Federal policies affecting the preservation and maintenance of our State and national infrastructures.

As State Treasurer, I am responsible, among other things, for the overseeing and executing of multi-billion dollar bonding programs in the State of Connecticut. And as Treasurer of a beautiful and much-blessed State, but one that is experiencing its own share of fiscal problems, I am very much appreciative of having this opportunity to speak with you today and the members of the Committee on a matter of great, great concern to all of us—that is, our aged and ailing State and local infrastructures.

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[1] See p. 58 for Mr. Borges' prepared statement.

We all know that the stakes are high, and as Chairman Sasser so aptly noted in his kind letter of invitation to me, without an adequate infrastructure, no economic activity is truly possible. And as he also noted, the degree to which economic activity is possible is directly linked to how adequately the infrastructure can sustain that activity. As you so well know, we in Connecticut understand that relationship and are, in fact, in the midst of an ambitious, 10 year, $6.6 billion program whose purpose is to ensure that the State's infrastructure remains viable.

The main portion of that infrastructure program, so far, has had to do with the maintenance and rehabilitation of our highways, roads and bridges. But we in Connecticut are also concerned about infrastructure in the broader context, and that is, infrastructure including water and sewage plants, sidewalks and curbs, public buildings, dams and flood control facilities, solid and hazardous waste disposal, as well as air, rail, bus and water transportation facilities.

I am sorry to report this morning to you that from our State's perspective, Senator, the primary role of the Federal Government in State and local infrastructure renewal has largely been one of both abdication and complication. The only exceptions are in the area of transportation, where the Federal Government has continued to act as our partner, and in the area of pollution control, where Federal contributions are helping to some extent to capitalize State pollution control revolving funds.

Yet an adequate and well-planned infrastructure is essential not only to commerce, but also to human communication, human health, and, indeed, human happiness. Those of us gathered here today have an opportunity to emphasize that the infrastructure, uniting the economy and the ecology as it does, must not be sacrificed or neglected for apparent short-term economic gain. Prudent investment in infrastructure cannot be sacrificed, however great our budget deficits are. When bridges, streets, and water pipes fall apart, the economy begins to fall apart, and the public health and the public safety can also be threatened.

As we all well know, the infrastructure crisis is severe; the costs of prudent investment in infrastructure are extremely high. And as you have already indicated, Senator, the National Council on Public Works Improvement has called the infrastructure, and I quote, "barely adequate to fulfill current requirements and insufficient to meet the demands of future economic growth and development."

The Council has also estimated that the costs of meeting infrastructure needs this year nationwide will be double the $45 billion those costs were in 1985.

On the local and State levels, the costs are equally staggering. Yet far from helping States meet the challenge of doing the financing they must do to pay for maintenance and improvements to aging infrastructure, the Federal Government has made the challenge tremendously difficult, if not impossible, to meet.

The prime culprit is the administrative nightmare caused by certain requirements of the 1986 Tax Reform Act, about which I will say a little more later. Another culprit is the Federal Government's apparent determination to limit local governments' access to the tax-exempt marketplace.

I will explain in more detail in a moment, but first let me give you some background about the situation in my home State.

As you so well know, not so long ago Connecticut was given ample and tragic proof of just how inadequate our infrastructure was becoming—how old, decrepit and neglected it was.

On the evening of June 28, 1983, a major bridge—that has been mentioned several times already this morning—carrying a major section of the Connecticut Turnpike over the Mianus River in Greenwich suddenly and silently collapsed, without warning, causing three people to plunge to their deaths in the waters below.

It was a horrifying tragedy that awakened everyone in Connecticut to the fact that our roads, highways and bridges needed immediate attention.

The deaths of three innocent people were a grim and unwelcome reminder that Connecticut was reaping the whirlwind of years of neglect and deferred maintenance of our roads and bridges.

Fortunately, Connecticut's Governor, William A. O'Neill, is a foresighted individual. On April 12, 1983, he had announced—even before the Mianus River tragedy—that he was forming a special Governor's Task Force on Infrastructure.

The Governor directed the task force, composed of members of State and local governments and the private sector, to develop a coordinated strategy for infrastructure improvements.

With the collapse of the Mianus River Bridge on June 28th, Governor O'Neill, to his everlasting credit, directed the task force to place special emphasis on infrastructure issues that directly affect the public safety.

Almost immediately, the State hired outside financial experts to work with us on a plan to deal with the highway and bridge repair problems. The task force also surveyed the condition of all public works, public buildings, roads, bridges, dams, and other such structures, and began to study ways to repair them where needed and to pay for the repairs.

The ultimate result was the development of a comprehensive 10-year, $5.5 billion plan for complete overhaul of the State's infrastructure. And of the $5.5 billion total for the 10-year plan, we in State Government set the State's share at $2.2 billion, with the rest to come from the Federal Government, based on the assumption that existing levels of Federal funding would continue.

So far, through April 1 of this year, Connecticut has spent $1.4 billion against transportation infrastructure renewal through a dedicated special transportation fund.

Naturally, it would be far easier on us if the Federal share of funding for this project were at, say, the 75 percent level.

Obviously, every State would like more Federal dollars for its infrastructure needs, and Connecticut is no exception.

And it is important to bear in mind that with fees, user fees and resources like gasoline taxes, transportation is perhaps the easiest portion of the infrastructure to fund. Asbestos removal, renovation of public buildings, and water and sewer projects are all far more difficult to find money for.

I have gone into some detail in describing our infrastructure renewal plan to demonstrate the depth of commitment of our State and the staggering costs of that commitment.

Meanwhile, a full decade of Federal retrenchment has sorely aggravated the fiscal burden our State bears in paying for other programs and services, including social ones. Like most other States with older cities, Connecticut has to find the money to pay for programs to address pressing social problems, even while having to find the funds for infrastructure improvements and other major budget items like education.

Here again, Federal retrenchment has hurt us. Everyone knows that polluted waters have to be cleansed, that the environment must be purged of toxic and hazardous waste oozing into the ground and the water and escaping into the air; yet the Federal dollars just have not been there for the States in sufficient amounts.

I would like now to turn my remarks to more detailed information, as Senator Sasser requested, on future infrastructure costs and the impact of regulation and tax policy, including the effects of the 1986 Tax Reform Act.

In terms of future infrastructure costs, Connecticut is a fairly small, compact and relatively wealthy State, as States go. Yet, as I have indicated, the costs of restoring and extending our infrastructure have been and will be enormous.

Our 10-year program now underway was originally set at $5.5 billion; its cost has risen with time and inflation to over $6.6 billion. A statewide billion-dollar pollution control effort is also under way. A half-billion program to relieve prison overcrowding has also begun.

And hundreds of millions more are being spent in Connecticut on local infrastructure projects, public schools, public buildings, colleges, universities, and on housing and economic development.

Meanwhile, the State's share of the transportation infrastructure program has grown to $3.1 billion, financed by a dedicated fund that receives all gasoline tax revenues, motor vehicle fines, and motor vehicle fees. The fund pays the debt service on special tax obligation bonds that are issued to finance the construction projects.

The other programs I mentioned are funded by ordinary general obligations. There are no gimmicks and no shortcuts, because as you are well aware, construction projects require a tremendous amount of cash.

Connecticut's capital budget has grown to—and through—the billion-dollar per year mark. This scale of investment cannot be sustained indefinitely by a State as small as ours. The situation is aggravated by the fact that local capital investment needs are equally great.

With respect to the impact of Federal regulation and tax policy, as I noted earlier, the Federal Government has continued to act as our State's partner in funding transportation programs. In the area of pollution control, Federal contributions are helping to capitalize State pollution control revolving funds. Otherwise, the Federal Government has abdicated virtually all responsibility in the State and local infrastructure renewal programs and has vastly complicated the State's efforts to pay for needed programs.

Meanwhile, the Federal Government has also walked away from housing assistance, from community development projects, and from economic development. Nor is any real assistance available for prisons, school construction, university construction, or construction or renovation of public buildings.

As to the following questions—Will State governments be able to meet the financial requirements of maintaining and developing needed infrastructure programs? Have new rules and regulations made the initiation and management of tax-exempt bond issues simpler or more difficult for State and local governments?—the simple answer, in plain English, is this: States cannot meet the challenge by themselves. And in Connecticut, at least, as a result of tax reform, we have had to go through prolonged, expensive, and totally unnecessary legal and financial contortions to try to finance projects at all.

Specifically, the problems created by the Federal Government in recent years are as follows:

First, the States' need to comply with the requirements of the Federal Tax Reform Act of 1986 has created a hugely unproductive administrative tangle.

The State of Connecticut alone must spend well in excess of $1 million per year to collect data on, and have bond and tax counsel analyze, each of the thousands of projects paid for by our general obligation bond issues.

When we use bonding to raise money to pass through to local municipalities, the arbitrage requirements of the 1986 act are nearly beyond belief. Unless all such pass-through funds are invested in tax-exempt securities that are not subject to the alternative minimum tax, we must track expenditure and investment earnings on those funds until the ultimate recipient has fully expended them.

Such tracking for the more than 1,000 projects currently in progress would be absurdly expensive, and it is.

In order to cope with the 1986 tax act, we in Connecticut instead have set up a special Tax-Exempt Proceeds Fund, with appropriate safeguards on deposit and expenditure, in order to keep the pass-through money flowing.

While I am proud that Connecticut is the first State to set up such a fund, its set-up and operation has been an expensive and labor-intensive process with absolutely no reason to exist other than to meet the Federal arbitrage requirements.

Second, the requirements that apply to the Clean Water Fund and to other pooled and revolving loan programs add more major expense and more difficulties.

Most orderly construction assistance programs advance money as work progresses. The pooled loan requirements imposed on us demand that we advance all of the money raised through bond proceeds within 6 months, or that the bond proceeds be yield-restricted.

The yield restriction requirements are cumbersome and expensive to administer. The arbitrage provisions relative to revolving loan funds require that every dollar be traceable back to the original bond issue, so that each time it revolves back to the fund an arbitrage calculation must be made. The alternative—yield restriction—erodes the value of the fund to absolutely no one's benefit.

I am going to conclude with the following: Third, while the Federal Government has walked away from housing assistance and has greatly reduced economic development assistance, the unified volume cap on so-called private activity bonds and other limitations on bond issuance for those purposes have severely limited the ability of States and cities to fill the void.

Connecticut has had to issue close to $100 million of taxable general obligation bonds—again, in very large volume—to maintain housing and economic development programs entirely on its own.

So, in general, at a time when infrastructure development and renewal needs are growing, the Federal Government has not only reduced the assistance it provides us in those area, but it has also added mightily to the costs and complexity of State and local efforts to meet their own needs.

To respond to the last of Senator Sasser's questions, in my view it is fruitless to look to the private sector for significant relief. Certainly, private industry has a role to play and a stake in making our communities better places to live and work, including helping with infrastructure improvements where possible and feasible. But I am not so sure that would work.

The prime responsibility for maintenance of infrastructure, because at the bottom it affects the public health and safety, must rest with Government. And State and local governments increasingly are in serious need of Federal help.

With respect to access to the tax-exempt bond market in order to provide the services the public requires and deserves, States and municipalities must continue to be permitted the access to the tax-exempt markets.

Over the past 2 years, that access has been ravaged by a series of legislative actions that, in the name of revenue generation, or in the alleged interest of ending so-called abuses—and, indeed, there have been abuses. I can say, Senator, that in the State of Connecticut we have not had a single instance of the abuses that have been recalled, that these new regulations have imposed a significant burden on States and municipalities that far exceed any benefits that I can think of to the Federal Government.

Moreover, this spring the U.S. Supreme Court overturned a 100-year precedent in *South Carolina* v. *Baker* by saying that the issuance of tax-exempt debt was no longer constitutionally guaranteed.

I strongly urge this Committee and the tax-writing Committees of Congress to become more familiar—and I think this hearing will help—with the considerable problems created by these legislative and judicial trends, and to make preservation of the tax-exempt bond market a major priority.

Congress and the present administration have the authority and the opportunity to dictate the future of public finance. This must include setting an agenda for legislation having to do with tax-exempt financing, helping to guide the promulgation of Treasury regulations dealing with this issue, and, in general, defining a national policy that emphasizes the importance of tax-exempt financing in meeting State and local infrastructure.

I am directing my comments to you today in this Committee not only in my capacity as State Treasurer of Connecticut, but also as an officer of the National Association of State Treasurers, an organization of State financial officers which has endorsed the points I am making.

Both the association and I invite and encourage this Committee, and any others in Congress, to work with us as State Treasurers to develop new policies or procedures affecting our ability to issue bonds and otherwise manage public debt and financing.

Only through such a cooperative effort will there be sound policies that more fairly balance the needs of State and local governments with the needs of the Federal Government.

Once again, I appreciate having this opportunity to appear before you, and I applaud you, Senator, and Senator Heinz and all of you, for giving us this opportunity to share with you some of the difficulties that those of us in State Government have in this area.

Senator **LIEBERMAN**. Thank you, Mr. Treasurer. That was a very helpful statement, particularly about the impact of the 1986 act on you and finance officers around the country.

I would now ask Secretary Yerusalim——

Senator **HEINZ**. If I may, since Secretary Yerusalim does serve as Secretary of Transportation for the Commonwealth of Pennsylvania, Mr. Chairman, prevail upon you to have the honor of introducing him?

Senator **LIEBERMAN**. It would be my honor to give that honor to you.

Senator **HEINZ**. Mr. Chairman, it is a great honor, a high personal privilege, to introduce to you Mr. Howard Yerusalim, who has been serving with distinction as the Secretary of Transportation for the Commonwealth of Pennsylvania.

Mr. Yerusalim, we welcome you. We thank you for being here, and we look forward to your testimony.

I thank you, Mr. Chairman, for your very kind courtesy.

Senator **LIEBERMAN**. Thank you.

Please proceed, Mr. Yerusalim.

TESTIMONY OF HOWARD YERUSALIM, SECRETARY, DEPARTMENT OF TRANSPORTATION, COMMONWEALTH OF PENNSYLVANIA [1]

Mr. **YERUSALIM**. Thank you, Senator Lieberman and Senator Heinz, for the kind introduction.

I am Howard Yerusalim. I am Secretary of the Pennsylvania Department of Transportation, and I am also chairman of the Pennsylvania Turnpike Commission. I am pleased to be here. I will not read my entire statement, as was requested.

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[1] See p. 74 for Mr. Yerusalim's prepared statement.

Let me start with a general statement, and then I am going to turn to the questions that were addressed to me by Senator Sasser.

Infrastructure involves many different issues, as indicated earlier in the hearing. As secretary of Transportation, I am going to limit my remarks to the transportation area.

We are nearing the end of the interstate era. For the last 33 years, we have placed major emphasis on completing the interstate system. I am pleased to say that in Pennsylvania, the entire 1,500-mile interstate system is either complete or under construction. However, now we have a major task. Much of that system is mature—that means old to some of us—and needs major restoration work, and I think we must turn our emphasis from building these new highways to restoring the infrastructure that we have in the highway and bridge area, as well as the transit area. Transportation is too important for the economy, the safety of our citizens to not address it in a responsible manner.

With that, I would like to turn to the questions that were addressed to me. The first had to do with the Federal, State and local roles, and I will read the question and then kind of paraphrase my answer.

What should be the roles of local, State, and Federal Governments in planning, building, maintaining and financing infrastructure? Well, there is a role for each of the three entities in this, and I think the role has been very successful in the past. I have had very successful relationships with the Federal Highway Administration and with the Urban Mass Transit Administration. However, as a member of the American Association of State Highway and Transportation Officials, we are trying to redefine that role.

I strongly believe that we should continue to be partners. However, I believe the States are becoming more capable of running their own programs. I think the Federal role should be revised so that they are not policing our projects and not setting standards and looking as to how we meet those standards. Rather, they should be involved in issues of national significance and systems of national significance.

Let me give an example of one of the things that Pennsylvania has done. Senator Heinz has already mentioned it. In 1982, we passed The Billion Dollar Bridge Program. We called it the Billion Dollar Bridge Program because it included a thousand bridges for $1.4 billion. And if we called it the $1.4 Billion Bridge Program, it would have sounded funny.

We had a dedicated tax for that program. It was found unconstitutional. It was replaced within 2 weeks of finding that it was unconstitutional. So we have taken the initiative at the State level. Through that program, by leveraging it with the available Federal funds and local funds and some private funds, we have been able to build about 1,000 of those bridges for about $1.2 billion since that time. With continuing that program, we will be able to rehabilitate or replace about 200 bridges a year for about $200 million each and every year.

Again, let me say that because the State and local governments are improving their capabilities to handle these programs, we should be reducing the Federal role in the details of the project review, et cetera. However, I do think that we have to continue the Federal role with respect to financing.

Let me give you a few examples, especially in the transit area. Federal capital operating systems to Pennsylvania transit systems has declined from $379 million in 1980–1981 to $155 million in fiscal year 1987–1988. That is a 60 percent reduction. There is $5 billion in the transit trust fund that is being held for deficit reduction, many believe for good reason, but it is not being held based on the fact that there is not a need for transit infrastructure improvement.

In fact, in Philadelphia, we have the Southeastern Pennsylvania Transit Authority. They have had a study done internally and externally by a nationally renowned consultant, and they have identified a $5 billion need for capital investment.

While State funding for operating assistance has increased in the last 10 years from $76 million to $208 million, or a 3-fold increase, Federal subsidies have decreased from $64 million to $27 million that is anticipated next year, reduced by more than 50 percent. In addition, Federal capital assistance for SEPTA has gone from a high of $172 million several years ago to $91 million last year, a drop of approximately 50 percent.

With a $5 billion need and with a reserve in the user-supported transit trust fund, I think the Federal Government must play a larger role in revitalizing our transit infrastructure.

The next question was: Under current policies, do you have the capacity to meet these new responsibilities? That is, the States taking over the programs. I will answer in one word: Yes.

What policies work well and what changes do you recommend? Well, overall, I think the Federal-State-local partnership works very well. I think the user fee concept of funding transportation improvements also works very well. However, I think the Federal Government must have a full commitment to completing and restoring that interstate system that we started 33 years ago.

If we look at the current authorizations, we will find that the Federal authorizations in the current Surface Transportation Assistance Act are $3 billion short of the needs nationwide to complete the interstate system. In Pennsylvania, we have actually borrowed the funds to complete the interstate system and we want to be sure that the Federal Government that entered into agreements with us when we borrowed those funds does, indeed, provide those funds to us. And I really have no doubt that they will, but I thought it was an important point to bring out.

With respect to changes, I think we need greater flexibility. We need design standards that the States can adopt and they can modify for different types of roads as they see fit. We need to be better able to transfer funds among different categories of highways, from the primary highways to secondary to urban, even to bridges, as we see fit. We need to eliminate the sanctions that we are threatened with due to issues unrelated to transportation, such as the clean air problems that we presently have. And we have to look to broader use of tolling.

I would also like to see a needs-based allocation of interstate restoration funds. Right now, interstate restoration funds are based on lane miles and vehicle miles, but not based on the amount of trucks that use the interstate system. As we all know, the heavy trucks are the ones that do the significant percentage of the damage to these highways.

Finally, I endorse giving States credit for their initiatives. Again, let me go back to the Billion Dollar Bridge Program that I mentioned before. I want to applaud Senator Heinz for his foresight in introducing a bill that would provide more funds for bridges and would give credit to those States that have taken their own initiative to provide more than the normal ratio of matching funds. In fact, we are funding much more than 50 percent of our bridge program each and every year.

What is the role of the private sector? Again, let me repeat, I believe in the user fee concept. I strongly endorse releasing the $14 billion that is in the Highway Trust Fund, again being held for deficit reduction reasons, and I understand the problem that you have with the Federal budget. I also oppose the use of a gas tax for deficit reduction, which has been talked about recently. However, I also believe that developers should pay a fair share of the cost for improvements to transportation systems that are caused by their development. And we are doing that in Pennsylvania, and I will give a few examples at the end of my testimony.

What are the possible negative impacts of private participation on infrastructure public policy decisions? I like to call it "the rich get rich and the poor get poor." When you get to the rich communities, they have the capability to provide matching funds for projects, and we have to be very careful that we do not take our limited Federal and State funds and only provide them in those areas where the developers or the local governments, because they have a booming economy, are able to match those funds. We have to be careful to see that the distressed areas also receive our transportation funds so that they can open their markets for new economic development.

With respect to improved intergovernmental cooperation, the question is: What steps should be taken to improve intergovernmental and public/private partnerships to promote more efficient management of resources? I think the first thing we have to do is better define the roles of the Federal, State and local government, and I have talked about that a little bit earlier in my testimony.

We must work together to define solutions, and we must recognize that mobility is the key. We have to stop this war between highways and transit. When we get into an urban area, if transit is the solution, we must utilize our limited funds for transit rather than saying they can only be used for highways. And I think this is something that we must address in the future.

Let me give a few examples of some of the private involvement that we have had in Pennsylvania. In eastern Pennsylvania in Chester County, there is an intersection of U.S. Route 202 and traffic Route 29. There is a Great Valley Corporate Center, which is a major corporate center with much high-tech type of industry locating there. A major developer in the area built the first ramp for $3.5 million for a new interchange. He actually built that several years ago. In June of this year, we will be opening bids for the rest of that $20 million project, funded, again, in a partnership between the State and a local development district through the municipalities that will be impacted by the new roads.

Another example is the Thorn Run interchange, which is an interchange on the parkway leading to the Pittsburgh International Airport. It is a $6 million project. It involves $3 million in State funds, $1 million in Department of Defense funds, and $2 million from a transportation authority. This project was recognized as the most innovative project in the entire Nation by the Federal Highway Administration last December. By opening up this area, there will be 7,600 new jobs adjacent to this interchange by the year 2000. So I think it is an important project.

The last example I wanted to give is the new Midfield Terminal at our Pittsburgh International Airport. We are building a new terminal. It is going to cost close to $600 million. It has county funds, it has State funds, and it has Federal funds involved in that effort. But there is another issue. We are building a new terminal that is not right adjacent to the existing road, and we have to build a new road to get to the new terminal. Well, that new road is going to cost about $100 million, and the Department of Transportation has agreed that they will, in fact, fund that road. The county, which owns the airport, will be providing most of the right-of-way. Again, we will increase the number of jobs related to that airport by 10,000, and we will also add about 4,000 jobs through opening up the land adjacent to the new road for development.

But in the cooperation area, let me stress something that occurred. Three or 4 months ago, I was a little bit concerned about whether we could build that road and not do damage that was unwarranted to the wetlands that are located there. We have a mine fire located there also. We sat down in cooperation with six agencies—three at the Federal level and three at the State level: the Environmental Protection Agency, the Corps of Engineers, and the U.S. Fish and Wildlife Agency at the Federal level; the State Department of Environmental Resources, the Fish Commission and the Game Commission at the State level. And what seemed like a major problem 3 or 4 months ago has reached a point where all 6 agencies, as well as our transportation agency and the county, have agreed on a location, have agreed on the type mitigation efforts that we will be making, and that highway will occur with mutual agreement.

Those are just a few of the examples, a brief outline of my testimony, and I thank you for having me today. I will be glad to answer any questions you may have.

Senator LIEBERMAN. Thank you. Again, the testimony was very helpful from the front lines.

Because Senator Heinz, as I too have found in my first 4 months in this office, is required to be in two places at once—he is in the middle of a Finance Committee hearing as well—I would therefore like to ask him to begin the questioning of the two witnesses.

Senator HEINZ. Mr. Chairman, thank you. I will not impose on your generosity overlong, but I do have one or two questions for Secretary Yerusalim regarding a couple of the comments he made in his testimony.

Howard, one of the things that I think you said, either in your verbal testimony—certainly in your written testimony—is that there are many States which are demonstrating their ability to launch major infrastructure projects on their own. My question to you is: Could you give us some examples? More importantly, what is it that those States do? How is it that they have the capacity to do it?

Mr. **Yerusalim**. Well, I cannot speak for other States, but I can speak for Pennsylvania. The one project I mentioned that will have no Federal funding, other than some special funding for an interchange to provide special access, is the Southern Expressway. We have determined that that highway is needed. The normal Federal funding does not provide the funds to do that.

The other thing that we are doing more and more is we are working with the private sector. I mentioned the one project in Chester County, the one project in Allegheny County. We are finding that developers realize that they are going to gain significantly. Municipalities recognize that with a new access provided by a new highway they are going to gain tremendously in the future. As a result, they have been willing to start assessment districts and other ways where they are providing the funds in the short range, when they know that through the taxes that will be coming to them in the long range, they will be paid back double, triple, quadruple, maybe even 10 times.

Senator **Heinz**. One of the things you mentioned verbally, as well as in your statement, was that the reason we are able to have, as you put it, a conservatively estimated Billion Dollar Bridge Program is because there is a dedicated source of revenue for it, which is essential.

One of the characteristics, as I understand it, among those States that have gone beyond Federal monies to do a lot of bridge and highway building on their own, like Pennsylvania, is they typically have dedicated sources of funding as opposed to relying to a substantial extent on general revenues through a State budget. Is that an important factor in encouraging States to go beyond being driven only by Federal matches?

Mr. **Yerusalim**. Yes, it is. As you know, Senator, we do have a dedicated motor license fund that can only be spent on highway-related purposes. But we saw the bridge problem back in 1982 as a major infrastructure problem, and we addressed that with our legislature and had almost unanimous support for that program. And they liked it so much, by the way, that they passed two more capital budget bills, and the program now has 5,067 bridges for $3.6 billion. We are hopeful that with the bill that you are proposing we might be able to do more than that 200 bridges a year for $200 million. But the fact that we had a dedicated source for bridges is what made that program work. Our legislature bought it unanimously because everyone had a stake in it. We could show them what would get done if they passed the dedicated source of revenues for that program.

In fact, one of the first issues that I had to face—I guess I should say Governor Casey had to face—was when the U.S. Supreme Court ruled that the axle tax that started that program was unconstitutional. And I would like to congratulate our State legislature, because I met with the Governor and we kind of set up the strategy, and then I met with the legislative leaders. Within 2 weeks, they had actually gone through both Houses and passed a replacement tax for the tax that was found unconstitutional—almost unheard of in the history of most legislatures.

Senator HEINZ. I join in your commendation of our State legislature. I think that was an absolutely remarkable, record-setting achievement. And I await the day where the House and Senate of the United States of America can do anything in 2 months, let alone 2 weeks. That will be the day.

You made another interesting comment about the potential problem of the rich getting richer and the poor getting poorer. Under our current highway program, that appears to be what is happening, in the sense that California—which is alleged to be a pretty well-to-do State—gets 46 percent of its highway money from the Federal Government, and Arkansas gets 28.9 percent.

It seems to me that, nonetheless, Arkansas ought to be commended—and I am sorry Beryl is not here. As he pointed out, they get about 47 percent of their money from their motor vehicle or fuel taxes. And I suspect they have a dedicated source of funding. They would presumably do better under a system such as I have proposed, if we extended it more broadly than just bridges. Would that be the case?

Mr. YERUSALIM. That would be the case if they had the funds, which it appears they do, to match the additional Federal funds. The same has been suggested by Secretary Skinner for transit, and we have a significant problem, as I pointed out, in transit, especially in the southeastern part of the State. It would be very difficult in Pennsylvania for us to come up with a higher percentage match. I think that setting that criteria in that case is much more difficult, and there is a reason for it.

Transit in Pennsylvania does not have a dedicated funding source. So it comes out of the general fund, and it competes against education and welfare and all the environmental issues that comes out of the general fund. And when you ask different individuals or if you ask different U.S. Members of Congress where is their priority—is it transit, is it environment—transit does not seem to come to the top of the line. Because of that, it is being short-changed.

Senator HEINZ. It is very true. And this is a little off the subject that I was going to question you on, but I think it is fair to state that among the States with major urban mass transit systems, which are a dozen or so States, Pennsylvania is, for all intents and purposes—and the qualification is because of the State of Massachusetts, which I will refer to later when relevant—the only State that does not have a dedicated source of revenue for mass transit.

That is our own political problem—and there is no way that Connecticut and the other States can help us solve it. But it is a serious problem. And SEPTA, as you have testified, and Lou Gambicino have a major problem that was just added to by a local judge the other day.

The question I would like to finish up on, Mr. Chairman, is this. In spite of the fact that States such as my own or Arkansas would do better under what I will call an incentive system, States like California would not oppose it. Instead, States like California say, well, we have the fiscal capacity to do more in the way of dedicated sources of revenue; we certainly need better transportation generally in California. And I am told that at least one, perhaps both of my California colleagues also are attracted to this same idea, albeit for their getting there by a different road or bridge.

Mr. Secretary, I thank you very much for your being here, for your questions, and, Mr. Chairman, I thank you for your courtesy.

Senator **Lieberman**. Thank you, Senator.

If I may, Mr. Treasurer, I want to ask you, if you can, to estimate the overall increase in the cost of public financing in Connecticut through the State Government as a result of the 1986 act. In other words, it seems to me from your statement and the other testimony we have heard today that there were some abuses in public financing, tax-exempt financing. But the Congress in the 1986 act threw out a net that has tied up a lot of other people and activities that were not a problem before. I wonder if you could bring some brush to that perception.

Mr. **Borges**. Thank you, Senator. We in the State of Connecticut have experienced significant additional costs associated with doing the financing since the 1986 tax act. Our cost for legal fees alone has exceeded well over a million dollars over what we had done previously, because bond counsel are now being asked to do a number of things they ordinarily would not have done under the old system.

Additionally, there are some administrative costs associated with tracking the arbitrage provisions. The arbitrage regs are beyond just a nuisance. They are fairly expensive for us, particularly for our pass-through expenditures. We are required by law to track those proceeds. And in particular programs like the Clean Water Fund, which is a revolving fund where the money goes out to the community and then it comes back, each dollar coming back we must re-loan within 90 days or track the rate on the original bond issue until the bonds are retired.

Just as a sort of anecdote, apropos of the new State legislative office building that was recently built, I recall having Bud Cohn, who is in charge of debt management for us, visiting with me and saying, "Mr. Treasurer, I think we have got a problem." And I said, "What is it?" And he said, "Well, I have got to have bond counsel go over the new legislative office building and measure out the space that the cafeteria is going to take." And I said, "Well, what is the problem with that?" What he said was essentially that the cafeteria is being run by a private enterprise, and that under the act a certain percentage of the activity, if it goes over what is allowable, you can no longer use tax-exempt financing to do it.

Well, the long and short of that is that bond counsel, who today are not necessarily very cheap, were over there on their hands and knees with a measuring stick to make sure that we had not gone over.

Senator **Lieberman**. It is a great story, and I think it shows how ridiculous the implications of the 1986 act have been.

Mr. **Borges**. Yes. I think for us the two major issues really have to be, as a State, is the difficulty associated with financing. Our ability to access the markets, having been severely impaired, thus required us to issue taxable debt, which is very, very expensive.

Senator **Lieberman**. It costs more.

Mr. **Borges**. The other is the arbitrage tracking, which, if you do not do it, has rather severe penalties associated with it.

Senator **Lieberman**. Again, there was in my memory no indication in Connecticut—and I will ask you to confirm it—that there were any abuses of the system that existed prior to the 1986 act.

Mr. **Borges**. Yes. The State of Connecticut, I can say—and we are very proud of that fact—has never utilized tax-exempt financing to build fast-food joints or to do other things of that nature. All of our projects have been ones that really provided economic development and did the kinds of things that were required.

Senator **Lieberman**. Let me ask you, and then Secretary Yerusalim, if he would want to comment on it. This is the Subcommittee on Federalism, and what strikes me as I listen to both of you is that one of the things that has been talked about recently in Washington is the possibility of an increase in the gas tax. The gas tax is used at the State level often, regularly, to finance infrastructure, particularly transportation improvements. What is your sense of the impact an increase in the Federal gas tax would have on the States' ability to finance infrastructure improvements?

Mr. **Borges**. We, as you know, Senator, have a dedicated fund, the special transportation fund, that is capitalized by a variety of components, a major piece being the gas tax. That is how we are able to raise the $5.5 billion for both highways and bridges. My sense is that it would have an impact. It is a dedicated revenue stream that we look to to be able to address debt service on that program, and I do think that an additional burden on it could have an impact in terms of flow.

Senator **Lieberman**. Mr. Secretary?

Mr. **Yerusalim**. I would agree with your comment. It would have an impact in several ways. First of all, it is already being done, to some extent, to the extent that there is $14 billion in that fund. If there were a major increase in the gas tax at the Federal level used for deficit reduction, it would probably reduce the revenues that the States receive through their current gas tax and other tax schemes because of the amount of fuel that would be used. I think it would have an impact on the use of fuel.

It also would have an impact on those States that are planning to have an increase based on a historically successful method of user fees for user purposes. If we had a 10- or 15- or 25-cent increase in the price of liquid fuels, it might be more difficult for those States that are planning a gas tax increase to have that gas tax increase enacted. So it almost has a double whammy on the transportation industry.

Senator **Lieberman**. Thank you. I have other questions, but I am mindful of the time. I appreciate your testimony very much. I think what I would like to do is to submit the questions to you and ask you to answer them in writing. Then we will include those answers for the record.

I thank both of you for coming up. Your testimony has been extremely helpful.

Mr. **Borges**. Thank you very much.

Mr. **Yerusalim**. Thank you very much.

Senator **Lieberman**. Let me now call on the panel of local representatives who are next to testify. We have the Honorable Burton

Stallwood, town administrator of Lincoln, Rhode Island, also representing the National League of Cities; the Honorable James Rout, commissioner of Shelby County, Tennessee, representing the National Association of Counties; and Ms. Virginia Rutledge, chief financial officer for the Massachusetts Municipal Wholesale Electric Company, representing the Government Finance Officers Association.

We thank each of you for taking the time to come up. If I may indicate again for the record, your statements have been received by the Committee and will be included in the record. We have got a total of about an hour left for this panel, and the other Ms. Rutledge. I would ask you to do your best to try to summarize your statements.

Mr. Stallwood, would you begin first, please?

TESTIMONY OF BURTON STALLWOOD, TOWN ADMINISTRATOR, LINCOLN, RI, ON BEHALF OF THE NATIONAL LEAGUE OF CITIES [1]

Mr. STALLWOOD. Thank you, Senator.

Senator Lieberman, I am Burt Stallwood, the town administrator of Lincoln, Rhode Island, and chairman of the Energy, Environment and Natural Resources Committee of the National League of Cities. I will curtail our remarks and keep within a 10-minute time frame for you.

I am here today to testify on behalf of the National League of Cities and the 16,000 cities and town across the Nation we represent on the ability of local governments to finance and maintain the Nation's infrastructure.

Public infrastructure deterioration has become more than a threat to the health and safety of our citizens. It has also begun to affect our economy. While devastations such as the April bridge collapse in Covington, Tennessee, highlight the urgent need for immediate attention to our infrastructure to ensure the safety of our citizens, a recent report by the Federal Reserve Bank of Chicago that was mentioned by Congressman Anthony—but I think it is worth repeating here—concludes that "a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, ports, airports, and other facilities which aid in the production and distribution of goods and services."

We believe our willingness to invest productively in the Nation's public infrastructure, to invest in our future, is critical to our ability to compete in an international economy. We now know, beyond any reasonable doubt, that the resources exist.

Shortly, we expect the President to sign legislation obligating the Nation's taxpayers to spend over $200 billion to bail out the Nation's savings and loan industry. That is a payment for past fraud, abuse, and failure, not an investment in the future.

We are here today to address what should be more important priorities. We would certainly welcome the introduction of legislation to create an ITC, Infrastructure Trust Corporation, authorizing the issuance of $50 billion in off-budget bonds to rebuild the Nation.

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[1] See p. 85 for Mr. Stallwood's prepared statement.

Let me add that we at the local level are very aware of the Federal deficit and its impact on decisions made here in the Nation's capital.

We have felt the effects of the Federal Government's attempt to reduce spending and get the budget deficit under control. Our proposals reflect our awareness of the difficult deficit problem with which you in Congress are trying to grapple.

We believe there are seven guidelines the Federal Government should undertake to help cities and States rebuild the Nation's infrastructure:

One, no further interference with tax-exempt municipal bonds. Capital investment at the State and local level have been and are funded largely through the use of municipal bonds. Over the past 8 years, however, the Tax Code has been revised no less than 6 times. Every time the Tax Code is reformed, the ability of State and local governments to meet the infrastructure needs of our Nation has been further curtailed.

In 1984, the Federal Government effectively ended the concept of public/private partnerships. In 1986, the Federal Government effectively eliminated tax-exempt bonds. It left slightly taxable, more taxable, and fully taxable bonds.

Each and every encroachment has simply increased the cost of building, maintaining, and rebuilding housing, streets, airports, water, waste, and other public capital facilities. The so-called reforms have not only limited State and municipal authority to issue capital financing but have severely eroded the potential market for selling our bonds.

Two, use of effective and retroactive dates for tax-exempt municipal bonds. One of the most severe impacts on major infrastructure projects is created by the growing practice of individual Members of Congress proposing effective or retroactive effective dates in bills restricting municipal authorities to use tax-exempt capital financing.

The imposition of an effective date imposes a cloud over the ability of a city, town, or State to issue a bond for bond counsel must opine that the bond could become fully taxable to the holder, thereby reducing any incentive for its purchase.

I want to emphasize that we recognize and are willing to spend our day in court fighting for what we believe is appropriate public policy. We believe, however, that a practice which permits an individual in Congress to hold public policy hostage outside of a democratic process is unfair and damaging not just to infrastructure, but to public policy.

Three, creation of a coordination mechanism to assure that full implications of changes in law are considered and understood before being made. We see a desperate need for some mechanism to reconcile conflicts and to assess the implications of changes in law.

Increasingly, municipalities find themselves caught between conflicting initiatives from the Federal Government. Let us take, for example, the recent Clean Air Act proposals. We are perplexed to find Clean Air Act amendments that require reductions in vehicle miles traveled (VMT), approved by the same authorizing Committee that has jurisdiction over the highway program, which bases the allocation of highway funds on vehicle miles traveled.

Such actions penalize municipalities by reducing transportation—that is, infrastructure—resources if we comply with the provisions in environmental laws. We are not talking here about different Committee jurisdictions; both measures emanate from the same Committee. If these kinds of conflicts cannot be dealt with within the confines of one Committee's jurisdiction, you can imagine the trepidation we experience when conflicts cross Committee or departmental/agency lines.

Four, consistency in honoring legislative commitments. Ever-changing Federal commitments and appropriations wreak havoc with the stability necessary to ensure the needed financial commitments to infrastructure projects.

For example, in 1987, Congress approved amendments to the Clean Water Act which, in effect, phased out Federal grants for the construction of municipal wastewater treatment plants and created, as an alternative, a State revolving fund. We were assured that funding commitments would be adequate to ensure that these new revolving funds would be more than sufficient substitutes for the eliminated grants.

Funding for the program was cut slightly over $400 million in fiscal year 1988 and by $450 million in fiscal year 1989. Moreover, the administration is seeking to cut $1.2 billion for next year, and we note that the Environment and Public Works Committee is expected to reconcile significant savings, presumably at least in part from this program.

Even once an appropriation is signed into law, we have no ability to count on it. The House and Senate Appropriations Committees are considering administration proposals to cut current funding levels more than 6 months after they became public law.

The same can be said for both the Highway and Airport Trust Funds. Unobligated balances exceed $23 billion, and we continually find these trust funds "used" to reduce the deficit.

If Congress and the administration decide that it is more in the national interest to use these revenues to reduce the deficit, then they should be honest about it and take them out of the trust funds and reduce the deficit. The current practice of the subjecting these funds to the appropriations and Gramm-Rudman process simply means that they are less and less useful as investment sources to meet national needs.

Five, mandates. Congress must begin to prioritize issues. It must recognize that we can no more afford to implement every good and worthy idea at the local level than you can at the Federal level. If the Federal Government is not willing to assign and fund priorities, we will do it at the local level—painfully and haphazardly, and probably in a hodge-podge pattern that is inconsistent and counterproductive from one city to the next.

It is also important for the Committee to recognize that the Federal mandates preempt other infrastructure needs.

Most Federal mandates have merit, but the Federal Government cannot absolve itself of the responsibility to participate in accomplishing federally established priorities at the expense of essential local services and priorities. I cannot tell the citizens of my city that we will no longer have a police force or a fire department so that those resources can be spent on measuring for 84 contaminants in our drinking water supply. Those are not acceptable tradeoffs at the local level.

Six, fiscal capacity. In addition to prioritizing what has to be done when, the Federal Government must also assess the fiscal capacity of other units of government to fill the void created by reductions in or eliminations of Federal financial participation in meeting Federal objectives.

We have raised taxes and read that the Federal Government will not. Federal access to revenue sources is far more equitable, and Federal ability to collect taxes is far more efficient than ours. We believe that the Federal Government is at the critical juncture where it must decide to raise the revenues to fund its mandates or forget about having them.

Seven, study on economic competitiveness. The Federal Reserve study states that Japan invests 5.1 percent of its annual output into public facilities while the U.S. comparable rate is .3 percent.

We believe it would be helpful to determine comparable rates in our other major economic competitors, so that the Committee can assess existing national efforts and commitments. We appreciate your concern and interest in this issue, Mr. Chairman. We believe it has to be the foundation of the Nation's future, and we share the apprehensions that this foundation today is fragile and crumbling. And we know that rebuilding it will cost far more tomorrow than repairing it today.

Thank you.

Senator LIEBERMAN. Thank you, Mr. Stallwood. As a new member of the Environment and Public Works Committee, I am particularly struck by the insight you have of the way in which we are going in two ways at once and running into ourselves with the vehicular-miles-traveled provisions which through the Clean Air Act go down and through the highway funding go up. I will address myself to that.

Commissioner Rout, if you would, please?

TESTIMONY OF JIM ROUT, COMMISSIONER, SHELBY COUNTY, TN, ON BEHALF OF THE NATIONAL ASSOCIATION OF COUNTIES [1]

Mr. ROUT. Thank you, Senator. I want to thank you and our own senior Senator, Jim Sasser, for allowing us to come here today and testify. We appreciate very much this invitation.

I speak to you on behalf of the National Association of Counties, NACo, where I currently serve as the chairman of the Taxation and Finance Steering Committee. And we have submitted a full testimony, but I will keep my remarks as brief as possible.

Americans take for granted, as we have heard today, a safe and reliable infrastructure network, and we rely upon that resource every day. But only rarely do we question the fundamental soundness of it. This is unfortunate because, as you have heard today from other testimony, our infrastructure desperately needs to be shored up. The challenge that confronts us does demand, I believe, a Federal, State, and local partnership that is truly cooperative. The theme of your hearing today, I believe, shows that you all understand this, Senator.

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[1] See p. 100 for Mr. Rout's prepared statement.

County governments are key players in financing, planning, and providing infrastructure services. The demands on counties become greater as the suburbanization of America moves ahead. We recently at the National Association of Counties completed a program called "America's Counties: Public Works Leaders." It found that counties own 40 percent of the roads in America, 34 percent of the public airports, 23 percent of the local public transit systems, and we provide wastewater treatment for more than 30 million Americans and are responsible for about 40 percent of the landfills that are owned and operated by local government.

But that only tells part of the story, and as has been pointed out by some of the previous speakers, the traditional definition of infrastructure is often confined to public works projects only. We believe that there are billions of dollars worth of other critical public projects which provide vital services in our community, and we cannot function, certainly, without adequate roads and bridges and environmental facilities. But it is no less true with regard to the public hospitals of America, the jails of America, the schools, and the housing stock. An infrastructure proposal would really be incomplete without considerations of these issues. Like bridges, these facilities are in need of repair in communities across the country. Just last year in Shelby County, we issued $30 million in tax-exempt bonds for emergency housing.

Counties own over 1,000 of the Nation's public health care facilities which includes the public hospitals. One of the largest in the Nation is our public hospital, the Regional Medical Center. Also, as it relates to jails, almost 4,000 of this country's jails are owned and operated by counties. Of course, as you know, from your own experience with the rise in drug-related arrests, there is an increasing demand and pressure being put on these jails today and a need for new and expanded facilities.

As an aside, in 1982, we in Shelby County opened a brand new justice center. Some refer to it as a "glamour slammer" because of its nicety, supposedly. It was to last through the year 2000. As of Tuesday, we had 2,450 inmates in a facility built to last to the year 2000 and house a projected 1,200 inmates. So we are now spending $22 million to build new cells to solve the crisis that threatens our financial stability right there in our own county.

Evidence of infrastructure decay continues to mount. As has been heard, half of our Nation's bridges are deficient; more than 28 million Americans are not served by modern sewage treatment facilities; more than a million miles of highways will require resurfacing by the year 2000; and no one can fail to notice the congestion of our airports and our highways.

In our own home State of Tennessee, Senator Sasser pointed out in his opening remarks and some of the other speakers today what has happened in the last few weeks. Nine people have lost their lives in our State due to the weakening infrastructure. April 1 was the U.S. 51 tragedy that has been talked about where we had the bridge collapse with eight people. On April 22nd, a small bridge in

Anderson County collapsed killing the driver there. In both cases, these bridges had been inspected, and recommendations had been made for improvements. But, unfortunately, the improvements had not been made.

In west Tennessee, my portion of the State, 45 bridges are rated critical, 683 bridges are rated poor. Just last week, in Memphis, the State closed another bridge in a very highly populated area of our city in the north section.

These facts concern me greatly, as I am sure they do you and others. The people of Tennessee, as well as the people in every state of the Nation, should not have to worry that the next bridge they drive across may be the last.

Fourteen of 21 Tennessee counties have bridges that have ratings that far exceed the measurement for replacement. It is clear that the infrastructure of our State and of America needs to be repaired.

As to recommendations, the National Association of Counties, which is over 3,000 counties strong, proposes four major components which should form the structure of any comprehensive Federal approach to the infrastructure crisis: One, an intergovernmental partnership has been talked about; two, no further reductions in direct Federal grant-in-aid programs; three, a serious review of a workable tax-exempt bond policy; and the use of a Federal gasoline tax increase only for construction and maintenance of our transportation infrastructure, particularly the interstate highway system.

As it relates to the specifics, on the intergovernmental partnership, it is truly critical if we are to improve and maintain the country's infrastructure. Counties have reacted to the dramatic decline in Federal financial assistance and growing local needs by increasing our own revenues. As you know, such things as revenue-sharing, when they were eliminated, hurt us drastically. In some cases, we have had to cut some vital services because of those cutbacks at the Federal level.

Although we are committed at the local level to ensuring basic public services are available, we cannot do it without a good partnership. And we are bearing more of the burden alone today than ever before.

Secondly, I would like to go further and talk about the current joint budget agreement and its potential impact on infrastructure. The agreement calls for over $5 billion in new revenues, I believe. That new money must not come from the hides of local government. I know in the past, as you well know, that has been the case very often. Legislative proposals have been recently introduced that would affect investments and tax-exempt bonds, such as doubling the scheduled increase in the alternative minimum tax for corporations holding these bonds. Although these measures could have adverse effects on future infrastructure efforts, these "revenue-raising" proposals are currently being given, apparently, serious consideration.

NACo supports tax increases to reduce the deficit. I make that clear. But it is time the Federal Government looked elsewhere, we believe, for some of its moneys. Not taking needed Federal revenue out of our pockets will go a long way toward re-establishing an important intergovernmental relationship.

Direct grant-in-aid is the second point. Federal grants represent another cornerstone of any intergovernmental approach to infrastructure. Washington has cut these programs to State and local communities by almost 50 percent over the last few years, including general revenue-sharing, which I mentioned earlier, which many very small and rural counties used for infrastructure, and depended on for infrastructure. We can afford no further funding reductions in the existing Federal programs that address the infrastructure needs throughout America.

Specifically, we believe Congress should fund the Community Development Block Grant Program at $4 billion and provide sufficient funds to renew expiring Section 8 rental assistance, as well as extension of low-income housing tax credits and other housing recommendations which are included in our full testimony.

We urge Congress to fund the wastewater treatment construction grants program to the full extent of the authorization—$2.4 billion. Even that amount is woefully inadequate, we are told, when we review the needs. Only recently, the EPA revised its estimated cost of upgrading the Nation's sewage treatment facilities to meet the Federal standards to $83.5 billion. That sum is 17 times more than EPA's current budget.

We support funding for the Federal Aid Highway Program at least at the current funding level of $12 billion adjusted for inflation. In mass transit, our priority is maximum funding for operating assistance.

The third major component is the workable tax-exempt bond policy, a very crucial issue to all of this. As direct Federal grants have declined, counties have had to rely increasingly on tax-exempt financing to pay for public projects of the type I have outlined earlier. We recognize that many of the restrictions authorized in 1986 were directly related to major concerns of cutting back abuse and of saving money. To address these concerns, all level of Government—local, certainly—must work together to set priorities for infrastructure needs and to better define the public purpose for which tax-exempt bonds should be used. This is the thrust of NACo's policies and recommendations in the tax-exempt financing area.

I will summarize a little bit that tax-exempt interest must be free of income taxation in order to preserve the market and the demand for bonds. We support deleting tax-exempt interest from the alternative minimum tax as well as from the book income of corporations who invest in public securities.

Tax-exempt bonds used to finance facilities that are governmentally owned and operated—airports, docks, harbors—should be categorized as governmental bonds. And non-profit, 501(c)(3) facilities should continue to be eligible for tax-exempt financing, but only if they meet public purpose criteria; for example, providing care to the indigent and underinsured in our community and our Nation.

To further the Federal, State and local partnership in the environmental area, solid waste and other similar projects that require us to work with the private sector should be given special exemptions. It was talked about earlier of a cafeteria in a building. We are talking here of the current 10 percent private activity/benefit rule that we believe at NACo is too restrictive and recommend considering increasing that to as much as 25 percent.

The arbitrage rebate requirement imposes burdensome compliance costs on local governments, and we support narrow provisions that would allow arbitrage earnings for small issuers up to at least $25 million and exempt large issuers from the rebate if they spend their bond proceeds expeditiously and use their investment income to reduce project costs.

Other current proposals to impose limitations on costs of issuance fail to take account of the complexity of the bond issuance process. An arbitrage nationwide cap such as 5 percent does not recognize that costs vary across our country. We oppose such restrictions. However, we may consider mandatory disclosure of issuance costs as a compromise, as a good-faith effort to address the Federal Government's concerns the bond industry is making too much money, perhaps.

The Federal gasoline tax, in closing, is the final component to an overall infrastructure policy. The National Association of Counties opposes raising the Federal gas tax for deficit reduction purposes. The gas tax has been key to infrastructure development and to our highway system and should continue to be such. But the lack of Federal commitment to an intergovernmental partnership is particularly evident because the Federal Government is not spending, as you well know, billions of dollars on already collected fees which are allocated for the Federal-aid highway, for mass transit, for airport improvement programs. We believe these dollars should be released for those purposes.

In summary, we look forward to renewed intergovernmental partnership to ensure a safe and sound infrastructure for all of our citizens. We look forward to working with you and the others in the Congress and the Senate toward that end. Thank you, sir.

Senator Lieberman. Thank you, Commissioner. I know Senator Sasser was pleased you were coming. I am sure he regrets that he cannot be here, but, as you know, he is over on the floor of the Senate.

Mr. Rout. Yes.

Senator Lieberman. Ms. Rutledge, I know you have been a national leader in this field, and we are glad to have you here.

TESTIMONY OF VIRGINIA B. RUTLEDGE, CHIEF FINANCIAL OFFICER, MASSACHUSETTS MUNICIPAL WHOLESALE ELECTRIC COMPANY, ON BEHALF OF THE GOVERNMENT FINANCE OFFICERS ASSOCIATION [1]

Ms. V. Rutledge. Thank you, Senator Lieberman. I am here today representing the Government Finance Officers Associations, which is an 11,000-plus member organization comprised of government finance officials at all levels of State and local government. I am currently the chief financial officer of a public utility joint action agency in Massachusetts, but I have spent part of my professional career as finance director of the city of Austin, Texas, and also Memphis, Tennessee, where I did know and work with Commissioner Rout.

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[1] See p. 118 for Ms. Rutledge's prepared statement.

Senator **Lieberman**. Glad we could create a reunion here.

Mr. **Rout**. We are, too.

Ms. V. **Rutledge**. Right.

The difficulties that we are having with infrastructure I think have been discussed at some length by the other panelists today. Particularly, some of the difficulties that we are facing are at the same time the Federal Government is asking the States and local governments to play a larger role in dealing with this huge problem of the state of the infrastructure. We are also finding ourselves much more restricted in our ability to deal with the problems at the State and local government level, particularly with the issuance of tax-exempt debt. The restrictions, the requirements, the regulations that have been placed on us have made the issuance of the debt cumbersome, have made the issuance of the debt more expensive, and have certainly affected the market for the debt.

All of this rolls in together to make it more difficult for the State governments and the local governments to be able to meet their part of the bargain in terms of trying to build roads, to be able to improve bridges, to meet the requirements for wastewater, for water and all of these other requirements that we are being faced with.

I think you will find that the local governments have not been unwilling to try to meet their share of the burden. Certainly, they have spent vast amounts of money, much of it raised by tax-exempt bonds, to try to deal with the burdens that they are experiencing. Some of them are seeing substantial increases in various fees to pay for these.

Holyoke, Massachusetts, for instance, is working on a program to improve its water supply system. But over the next few years, they are expecting to double their water rates. Nonetheless, they are making the commitment, and you will find cities and counties making commitments like that all over the country at this point in time.

We do need help. We do need to be able to issue the tax-exempt bonds to make these burdens a little bit less.

I would like to deal primarily with some of the key problems that we see in this area. Certainly, the arbitrage rebate has been discussed at length today. It is probably the most intrusive and possibly the most costly restriction for the State and local governments that they are facing.

Let me give you an example from my own experience of how arbitrage, which seems to be considered like a four-letter word, is often used in the State and local governments. When I served as finance director of Memphis, Tennessee, we issued bonds on a fairly regular schedule to build streets and roads, to do bridge work, and all of the things like that. To the extent that there were any earnings over and above the cost of the interest rates on the bonds, those earnings went into one of two places. They either went to reduce the amount of bonds that had to, in fact, be issued to build the projects, or they went to reduce the debt service on the bonds so perhaps you could issue a few more bonds, build a few more roads, or improve a few more bridges.

We think a use like that, which is where the vast majority of the interest earnings off of the bonds goes, is certainly not inappropriate. It goes along with the overall programs that we are trying to implement, that we are trying to do, and that is, for the most part, where you will see people spending their arbitrage.

At this point in time, the interest income must be rebated if all of the proceeds are not spent within 6 months of the bond issue. You need to understand that most of the infrastructure projects cannot possibly be done in a 6-month period of time. Some projects take 1 to 2 to 3 years; a public power project may easily take 3 to 6 years.

There are many States and local governments that have laws that affect expenditures; contracting requirements, for instance, not allowing a government to enter into a contract until it has the funds on hand to be able to meet the contracting requirement. That is a reasonable requirement. That is a prudent financial practice, but yet it also means that it is unlikely that that government is ever going to be able to spend the proceeds within a 6-month period of time.

We at GFOA have tried to do some estimates on the cost of the arbitrage burdens. We have talked with other cities and governments to try to get a feel for the burden. For instance, in the city of Atlanta, which [illegible] issuing approximately $8 million a year for general obligation-type improvements, it is estimating that it is spending $2,500 per year per issue to try to deal with the compliance-related aspects of the arbitrage requirement. They estimate that over the next 20 years they are going to be spending a million dollars on that particular issue.

We have also made some estimates on the overall burdens to the State and local governments of the arbitrage, not only with the cost of the amount of money that is rebated, but also with the compliance costs in terms of getting the attorneys to be able to see if you are in compliance, to be able to make sure that you are doing the rebate properly.

Our estimate over a 5-year period, these estimates made in 1987, is that the overall cost is in the range of $1.1 billion to the State and local governments. We believe that is a conservative estimate. Yet the Joint Tax Committee Federal revenue gain estimate was, at most, $150 million for that same 5-year period.

We think the economics in terms of the burden to the State and local governments needs to be considered in weighing against the gain potentially to the Federal Government. Some of those simply do not equate out to be reasonable.

I think one of the greatest threats that we also have to face in the tax-exempt market is the gradual disappearance of investors who are willing to purchase tax-exempt bonds. The cumulative effect of the numerous changes is almost unparalleled uncertainty, greater volatility in the market for the tax-exempt bonds, and the almost unbelievable complexity in terms of trying to determine whether tax-exempt bonds are, in fact, a benefit for an individual consumer.

I have had some experience myself in simply trying to advise my own mother in terms of whether she should or should not buy tax-exempt bonds, given that she receives Social Security. It is a difficult issue. It is also difficult with insurance companies who now find their reserve requirements adjusted based on the amount of tax-exempt bonds that they are holding, banks who cannot deduct the cost of purchasing and carrying tax-exempt bonds except for small issuers, Social Security, which may be taxed depending on how much tax-exempt income you receive. These types of provisions make it very difficult to determine exactly what the benefit to any individual taxpayer may be.

There are additional proposals that have been suggested in terms of limiting the amount of tax-exempt interest that any one taxpayer can have, disallowances on tax-exempt income involving installment sales, the expansion of the alternative minimum tax preference to all bonds as opposed to just being imposed on private purpose bonds. And there is currently a proposal to attempt to supposedly simplify the adjusted current earnings provision but that would also create a greater alternative minimum tax burden on the State and local government tax-exempt issues.

All of these issues are very difficult to quantify in terms of their impact on the State and local governments. The general consensus is that the bonds which are subject to the alternative minimum tax are selling at approximately 25 basis points greater than bonds that are not subject to the AMT. For instance, on a $10 million bond issue over 20 years, that is $268,000 in increased borrowing costs, and that is simply multiplied by the number of bond issues over time and across the country.

First Tennessee Bank National Association has done some estimates on their experience on issues with the loss of the bank deductibility, and they are estimating that to be in the range of 30 to 110 basis points for any particular issue.

I think one of the difficulties that we are also faced with is what I would call mixed signals from the Federal Government in terms of what are the national priorities and the most efficient ways to do things. For instance, we know in some cases that doing low-interest loans, low-cost loans for energy conservation, can be a far cheaper way of dealing with the need for energy in this country and in reducing demand for building new power plants. Yet there is a private loan test that restricts the amount of consumer loans that can be included in any bond issue to 5 percent of that bond issue.

Well, in the power industry, if you are not building a plant because you are trying to do conservation, 5 percent can be a very, very small number and can restrict the overall ability to use this tool effectively.

There have been restrictions that have been placed them or attempted to have been placed, on revolving loan funds which would restrict the ability to use them for clean water requirements and the like. On the one hand, we find ourselves having certain Federal agencies that are suggesting we use vehicles like this, and on the other hand, we find other entities that are also trying to restrict our ability to use these vehicles.

We have the SEC looking at disclosure requirements at this point for State and local government issues, and increased disclosure is generally going to increase issuance costs somewhat. Yet we also have other Members of Congress who are looking at limiting issuance costs.

The Tax Code complexity in and of itself does increase the cost of compliance and the cost of issuance, yet, again, that is counter to trying to reduce the issuance costs.

The limitations on banks' ability to deduct the cost of buying and carrying tax-exempt bonds also is limiting their usage more and more in terms of buying these tax-exempt bonds. Yet the State and local governments have what I would consider to be an admirable record in terms of default, with perhaps the notable exception of WPPSS. Certainly, the banking system could use more stable, more trustworthy investments to be able to add a little help in that area.

We are asked to do more with less, and that typically means trying to develop good public/private partnerships and good public/private relationships. These are often a more efficient way to provide services to the citizenry at large, yet the Tax Reform Act has substantial restrictions on our ability to be able to enter into these kinds of relationships.

All of these are conflicting signals, and they do serve to confuse the State and local governments as to which really are the priorities that we are trying to deal with.

We at GFOA are working hard in this area to try to make sure that we educate State and local government officials so that they know how they really are impacted by these issues. We are also working with what we call a Public Finance Network that involves the State and local government officials throughout the country, public interest groups, many of them trying to get the State and local government officials to be aware of these issues and to be able to know how to communicate with their representatives, with their Senators, so that Congress will be more aware of how local governments are impacted by these different changes.

We have also been very involved in working with Congressman Anthony with the Anthony Commission in trying to make sure that the problems, the possible solutions—and we certainly are willing to come up with solutions that do not try to create abuses—so we are able to deal with this and be able to issue the bonds that we think we need at reasonable cost to be able to meet our needs in the infrastructure.

Thank you.

Senator LIEBERMAN. Thank you.

I must say the testimony of the three of you was very impressive. I appreciate it. And if I may say so from this perspective, the governmental entities that you serve are lucky to have you. I hope they agree.

Time is running. Let me just say one thing. I want to repeat something you said, Ms. Rutledge, because it seems very powerful to me. You said that you had estimated that the cost of complying with the arbitrage requirements for that 4-year period, 1987 to 1991, would be $1.1 billion.

Ms. V. RUTLEDGE. Yes, sir.

Senator LIEBERMAN. You also said that the Federal revenues that would be earned or saved during that period of time is $150 million.

Ms. V. RUTLEDGE. Yes, sir.

Senator LIEBERMAN. That is a pretty bad return on our money.

Ms. V. RUTLEDGE. We think so.

Senator LIEBERMAN. I agree. I would be interested, but not now, with your own sense of whether the experience for the 2 years of that estimate period, is running close to the estimate.

Ms. V. RUTLEDGE. We have not done a complete new study since then This was a 1987 estimate, so it was made 1 year after the act.

Senator LIEBERMAN. Right. I would be interested, as time goes on, and you could submit it in writing to the Committee.

Ms. V. RUTLEDGE. We will monitor it. I will be glad to provide you with that.

Senator LIEBERMAN. That is great.

Let me ask you each a quick question, and, again, I apologize for the running of the time. Your prepared testimony as delivered here has been very, very helpful. If you had one thing you would want the Federal Government to do to make this problem, both the infrastructure itself and the financing problem better, what would be your top priority for us? Mr. Stallwood, would you start? And then we will just go down the row.

Mr. STALLWOOD. Well, I guess from everything we have heard, it is just not from the National League of Cities perspective, but I guess tax-exempt financing would be the number one issue that we would like you to address that would allow us to help put the infrastructure back through tax-exempt financing. I guess that would be the one to me.

Senator LIEBERMAN. To pull off some of the restrictions that came on——

Mr. STALLWOOD. The arbitrage.

Senator LIEBERMAN. Okay. Ms. Rutledge?

Ms. V. RUTLEDGE. I would agree that being able to use the tax-exempt bonds and reducing some of the restrictions is one of the most important things that we can have, though I would point out that I include those restrictions that affect the marketability for the bonds, because they are as important as the arbitrage restrictions that we see directly.

Senator LIEBERMAN. Okay. Commissioner?

Mr. ROUT. I would concur. The tax-exempt area is the issue. I think, in addition, if there is one other thing, it is to make sure that local governments do not have to continue to absorb any more of the Federal cutbacks.

Senator LIEBERMAN. Great. Thank you very much. That is a pretty clear consensus. Thank you.

Mr. STALLWOOD. Thank you.

Mr. ROUT. Thank you.

Ms. V. RUTLEDGE. Thank you.

Senator LIEBERMAN. Our third panel is a panel of one, which is Nancy Rutledge.

Ms. Rutledge, thank you for coming, and thanks for your patience. I know that you are a nationally recognized expert and leader in this field, and we appreciate your deference to the public officials who preceded you. We will be glad now to hear your testimony and then have a little discussion.

TESTIMONY OF NANCY S. RUTLEDGE, FORMER EXECUTIVE DIRECTOR, NATIONAL COUNCIL ON PUBLIC WORKS IMPROVEMENT[1]

Ms. N. **Rutledge**. Good. Thank you, Senator Lieberman.

Being the last, mop-up witness is a humbling experience, partly because I have watched a lot of my best lines being used by some of the long string of very articulate witnesses today. What is more, there are relatively fewer people to listen to it. But on both counts——

Senator **Lieberman**. I want to say to you that as a freshman Senator, I empathize with your predicament. [Laughter.]

Ms. N. **Rutledge**. In some ways, that may well be an advantage. Since you have my prepared testimony, I would like to spring from that a little bit.

Senator **Lieberman**. Good.

Ms. N. **Rutledge**. And I will take a slightly larger risk in terms of what I plan to say here.

I have watched the emergence of the infrastructure in the last 12 months with an immense amount of interest. You know, when I left the Council in April 1988, we did get quite a bit of press attention with the publication of "Fragile Foundations." But, in fact, instead of just disappearing, as most Federal reports generally do, it has actually grown in importance. I would like to think it was all the fine work we did, but, indeed, I know the fact is because every single day people are stuck in traffic. They are watching this crud flow up on their beaches. I know Connecticut was witness to that this summer.

We are sensing that a lot of the basic systems are simply not working so well any more. There is a sense of fragility that I think is felt by people who would never even utter the word "infrastructure," much less listen to testimony like my own.

I earned my stripes up through local and State government on this issue, and so I have watched it and I understand very well the frustration of local government officials, in particular, who are on the firing line. But I am so frustrated by the fact that so much of the discussion is almost exclusively on the question of money.

I do not question at all the fact that we need more investment. The Council made, I think, a pretty strong statement in that regard. It was more rhetorical than quantitative, but it was still a centerpiece that we do need to increase our investment, in fact, up to 100 percent, if not more.

But I do not think anyone spends money on anything unless they value it, unless they understand it. And it is perhaps a stretch to say this, but I will try it. The fact that the American public has, in effect, collectively paused in the rate of investment, I do not think is just a matter of constrained resources. Certainly, there are a lot of other competing priorities. But part of it is I think a growing skepticism that the traditional manner in which we have provided infrastructure simply is not going to work. We certainly need more transportation facilities. Traffic problems in virtually every metropolitan area in this country, in fact the world, are horrendous. But nobody is willing to turn the entire planet into pavement.

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[1] See p. 157 for Ms. Rutledge's prepared statement.

Indeed, we have got to start thinking about how we get people from here to there, where people settle, where they decide to work in relation to where they settle, their expectations for getting from point A to point B. All of the tolerances in that have changed dramatically. We have changed as a society dramatically in the last 20 years, in the same period in which investment has gone down. Our economy is changing. It feels a lot less secure than it did once. We are facing dramatic new technologies in virtually all areas of the private sector and our lives that affect our demand for infrastructure. Our life styles have changed. Our expectations of the environment, our expectations of our infrastructure have, indeed, changed in a short period of time.

The upshot of it is not just that our infrastructure is aging and getting frayed around the edges, but it simply fundamentally does not address current needs. Now, whether or not all of those needs are justified or whether or not there are priorities we are willing to pay for are important questions. But I would posit at the outset that we need to go back first and begin to think about where we are heading. Infrastructure is just the means to get there. It is not the end. The structures, a soaring bridge, may appeal to our senses, but it does not necessarily mean anything to us, except that it gets us from here over to the other side of that river or whatever function a piece infrastructure carries.

Senator Lieberman. That is obviously a very provocative statement. Do you sense it is really a public pause in the substance as well as the financing question? In other words, a wonderment about whether, really, the answer to the pursuit of the better life is going to be achieved by more highways, for instance?

Ms. N. Rutledge. Yes.

Senator Lieberman. You do?

Ms. N. Rutledge. Yes, I do, very strongly. And I say that now, having stepped away from Washington, D.C., and gone back to a town of 2,500. It is part of a very growing metropolitan area in the mid-coast of Maine, so it is not immune from infrastructure problems. In fact, it has many of its own. But the question of infrastructure is really superseded by the question of place. What is it about where we live that means something to us? What makes it important? What makes it not just a productive place to live in terms of our industries and our ability to create jobs, but also a place that appeals to our senses and makes us feel proud we are part of it?

And when, indeed, you find communities around this country who have invested in infrastructure—and there is no one out there that I suppose would say that it is perfect, but there are communities who are justifiably proud of their systems. The reason they are is because they thought the investment there as leading to this larger vision, which is well beyond the scope of infrastructure. It has to do with our sense of place and our lives; you know, the things that we do value at the very bottom line.

I believe that that is where the discussion has got to be brought back to. Money is a part of that, but it is not the only part of it. How we make infrastructure, the construction of it, the technology and the development of it which is so sadly limited in this country.

We spend virtually nothing on that part of R&D, even while we are spending more than any other country in the world on our R&D overall.

Senator **LIEBERMAN**. Could you elaborate a little bit on that? Is that policy R&D or technological R&D?

Ms. N. **RUTLEDGE**. Well, I am speaking primarily of technological R&D, but it is meaningless unless it is coupled with policy.

Senator **LIEBERMAN**. Right.

Ms. N. **RUTLEDGE**. Unless it is coupled with the means of conveying technology into application.

I was impressed recently to learn about a project that the Electric Power Research Institute manages in North Carolina that is aimed at making all of these wonderful technological innovations mean something at the practical working level. You know, it is one thing to read about it in a book and have somebody give an eloquent lecture. It is quite another thing to build the software or to create the public wealth or to reduce the liabilities, or whatever the other impediments to innovation are, to make it work in your community or in, in this case, your electric power plant. But I think the same institutional obstacles in electric power plants are true in local government. There is frequently not the kind of technical resources or people power within the local public works department to really make use of ideas, to make it work better. It may not mean spending a lot more money. It may be possible to divert investment, to make the service work without actually have to spend money—the same level of money.

Senator **LIEBERMAN**. Right. Actually, I can offer you an example of this. I had a recent conversation about sewage treatment facilities. Obviously, there is an enormous national demand for money to improve sewage treatment, essentially to make water cleaner. And the fellow who was a professional in this area was saying to me that he was just thinking recently that it startles him that we are still making sewage treatment facilities the way we did, I do not know, 40, 50 years ago; that the technology is basically the same.

He expressed a little bit of skepticism as to whether that might be happening because people in the business, the professionals, are essentially just taking the same plans off the shelf and repeating them place to place. But sewage treatment is such a national, international need; in just the financial sense, there is an enormous market there. And you are right, at least based on this conversation I had, nobody seems to be asking the question about whether we can do it better and cheaper than we are doing it now.

Ms. N. **RUTLEDGE**. There are some other equally provocative questions about the land use questions. And those are not things that the Federal Government can certainly enforce or impose. I would hardly even venture the idea. But, still, from the bully pulpit at the Federal level, looking at State and local government, I think there is just a vast area of improvement there that would have profound implications for infrastructure demand. We could also look at the quantity of garbage we produce, not just in terms of more innovative ways of burning it or transporting it or whatever, but also perhaps imposing some incentives on the private sector to produce less of whatever those substances are.

I realize this is a dangerous word these days, but value-added taxes, some measure—and, again, whatever that is, I am not an expert in that area. But some way of building the cost of disposal right in at the beginning so that we, the consumers, have to make a choice when we buy something or demand something at the outset.

Senator **Lieberman**. Yes, it is interesting. In that field, people are beginning to talk along those lines, although it is very early in the preliminary discussions; whereas, I do not really hear it except for what you are saying now in the whole area of infrastructure. I appreciate your bringing the two together.

In your prepared testimony, you had some thoughts about, I believe you called them financial incentives to encourage—or to deter neglect of infrastructure. What are you thinking about? Can you elaborate on that? Obviously, that is part of our problem. We have neglected the infrastructure. How might we have avoided that neglect?

Ms. N. **Rutledge**. Right, Well, I was very encouraged a few months ago to learn that the New York City Charter Commission passed a provision—and it was passed overwhelmingly, 88 percent by the public—which demands that the mayor every year attest to what the city's infrastructure capital requirements are and what the maintenance requirements are and how much of those maintenance requirements are not being done.

Now, certainly the mayor is not forced to fund all of maintenance because obviously there will be other priorities that occasionally will have to deter it. But by the same token, he is at least forced to lay it out on the table that we are, indeed, doing 40 percent less, or whatever that number is, of our infrastructure maintenance requirements. So it becomes a matter of public record. And that is a first step.

There are other ways of building into the incentives; for instance, communities that do not do maintenance should be fairly penalized in terms of investment. In fact, even in the tax-exempt bond rate. Now, that, again, gets into the private sector. But if, indeed, the investment is not being taken care of, the capacity of that city to produce revenue or to produce user fees, whatever the source of revenue for those bonds are, is jeopardized. And to the extent that the investor community, as well as perhaps the accounting community, begins to recognize that—and I know that they have been struggling with that for several years. I believe it is still in some discussion—to build in at least as part of the financial bill of health to a community that they are doing their maintenance. And if they are not doing it, why not? And also, what is more, what are the implications for not doing it?

We know that certain facilities are very vulnerable to under maintenance. We have witnessed that, and I, having worked in New York City, saw firsthand what that meant. And to the extent that the public is made more aware of it, I think that is perhaps the best step forward.

Senator **Lieberman**. What would you like to say to us in the remaining 3 minutes?

Ms. N. **Rutledge**. Well, I hope, I just hope that you will keep talking about it and that you will keep pressing more people to bring this subject to the attention of the Congress. Because by doing so, you not only help educate Members and staff and the public, but also there is an opportunity to give some good will and support to local governments, because they are the ones that are making those choices to try to build the financial support and the public will to do things. And by at least having the focus here and the discussion here, it is a reference point that I think can be quite helpful.

But I guess it is equally important to me that this subject is not just money but that you are, indeed, talking about how we do infrastructure and what we are doing and why we are doing it, not simply just how we are paying for it.

Senator LIEBERMAN. Very strong point, and a perfect place to conclude. Sometimes it seems to me that these hearings are upside down. Maybe we should have started with you. Thanks for your written testimony, and thanks for the statement you have made, which is a great way to leave the hearing. I look forward to having the opportunity to talk to you at more length at some other time.

Ms. N. RUTLEDGE. Thank you.

Senator LIEBERMAN. Thank you all for being here. This now will conclude the hearing.

[Whereupon, at 12:28 p.m., the Subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX

STATEMENT BY CONGRESSMAN BERYL F. ANTHONY, JR. BEFORE THE SENATE GOVERNMENTAL AFFAIRS COMMITTEE

MAY 4, 1989

Thank you for this opportunity to speak before the Committee about the problems our nation faces in building and rehabilitating our infrastructure. What all of us want most is to keep this country from literally falling apart. Senator Sasser recently experienced the tragic death of 8 people in Tennessee when the bridge crossing the Hatchie River collapsed on April 1st. Senator Lieberman, I am sure you are familiar with the collapse of the bridge on Interstate 95 in Connecticut, in which three people were killed. Evidence of the failure of our sewer and garbage disposal systems washed up on East Coast beaches last summer. The shellfish in the Chesapeake Bay and along the New England coast have been contaminated, threatening public health and safety. These are graphic and tragic examples of the crumbling of this nation's infrastructure. They are tragic both in human and in economic terms.

In my own home state of Arkansas the results have been evidenced only in economic terms so far. A 1984 study of Arkansas' cities and counties showed $862.9 million of critical repair and replacement projects needed for streets, roads, drainage, bridges, and water, wastewater and solid waste disposal facilities.

Declining investment in infrastructure is a problem of national proportion. During the 1950s, 1960s and 1970s the federal government sponsored substantial investment in the nation's transportation and public works systems. We have outgrown those systems today and need a new federal commitment to national infrastructure programs. But the federal budget deficit overwhelms our ability to reinvest in the health, educational, public works and transportation systems needed if we are to be strong economically during the 21st century.

Faced with reductions in direct federal spending and restrictions placed on tax-exempt financing in the 1986 Tax Act, a number of my Arkansas constituents, including Governor Clinton, urged me -- because of my seat on the House Ways and Means Committee -- to take a look at the overall federal cuts in state and local government financing. In January of 1988 I put together the Anthony Commission on Public Finance to review the effects of the 1986 tax bill on the abilities of state and local governments to finance their increased responsibilities particularly in the area of infrastructure. During the past 16 months this group, made-up of state and local government officials and professionals from the public finance industry, has diligently reviewed the affects both of changes in federal program requirements and in tax laws directing their financing abilities. Their report should be ready within about a month. But let me share with you some of the things which I have learned during this process.

During the 1950s and 60s investment in the nation's infrastructure grew. States and the federal government both became accustomed to policies in which Congress and the Executive Branch mandated national standards for federal programs and helped finance those requirements. Dramatic reductions in federal spending for infrastructure arrived with the budget deficits of the 1980s. When President Reagan took office in 1980, public debt was $914 billion. By 1987 the debt grew to $2.3 trillion. Simultaneously President Reagan espoused what was known as the "New Federalism" -- let the states take back control of the federally mandated programs which belong at the local level.

I agree with the policy that many of these programs should be implemented at the local level. We in Congress must recognize, however, that federal mandates are more costly for states and local governments. We should acknowledge our share of the responsibility for financing these programs and particularly at a time when federal spending is declining, we should not restrict the ability of states and localities to raise revenues for important public purposes through the use of tax-exempt bonds.

Our track record of support for state and local governments during the 1980s has not been good. In FY 1980, funding for the Environmental Protection Agency's Wastewater Construction Grant Program was $3.4 billion. It dropped to $1.2 billion in the FY 1990 budget. Meanwhile the Clean Water Act has required all communities to achieve secondary treatment standards by July, 1988. The EPA itself estimated that 400 cities and towns would be unable to meet that deadline. Yet reauthorization of the Clean Water Act provided only $2.46 billion for what EPA recently estimated will require $83.5 billion to construct.

During the 1980s public transportation funding was cut from $3.527 billion to $1.523 billion. Transportation congestion increased dramatically and resulted in decreased productivity and competitiveness. The Federal Highway Administration says over 60 percent of the United States' paved roads and 25 percent of the interstate highway system need resurfacing or reconstruction. Thirty-five percent of the interstate system will have outlived its designed life by 1990, while 45 percent of the nation's bridges are structurally deficient or obsolete. If you drive to work on the Whitehurst Freeway here in D.C. you know how true this is.

A recent issue of the Chicago Federal Reserve Bank's letter concludes that countries which provide high public investment in infrastructure experience higher productivity growth. The letter says, and I quote, "thus a root cause of the decline in the competitiveness of the U.S. in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, ports, airports and other facilities which aid in the production and distribution of goods and services." End of quote. During the past twenty years spending on infrastructure in the United States has dropped from 2.3 percent of GNP to 1 percent.

This nation's infrastructure needs are staggering. For example, New York City intends to spend $57.3 billion on infrastructure during the next decade, while the NY/NJ Port Authority will spend over $5.8 billion during the next five years. The Metropolitan Transportation Authority will spend about a billion dollars per year during the decade. New York City alone will need about $80 billion in required investment between now and the beginning of the 21st century.

One of the most dramatic problems facing this country is the nationwide shortage of affordable housing. It is estimated that by the year 2000, 19 million people will be homeless in this country. Nevertheless, direct federal funding has been cut from $26.98 billion in FY 1981 to $7.851 billion in FY 1989. At the same time tax incentives to provide housing for just about anyone but the affluent have been eliminated.

Putting these reductions into perspective, during the period 1980-1987, federal aid to states and cities declined 37 percent in real terms. The Commerce Department says the proportion of federal spending going to state and local governments fell in 1987 to its lowest point since the 1960s. In Illinois, for example, local aid during 1981 was 18.9 percent federally funded and 13 percent state funded. In 1986, it was 10.5 percent federally funded and 13 percent state funded. Thus, during the period, local government revenues rose from 62.1 percent to 71.3 percent to meet the shortfall.

State and local governments, unable to abandon investment in local infrastructure, have attempted to pick up where the federal government left-off. States currently provide 70 percent of all infrastructure investment, but this is primarily to cover operation and maintenance, not new construction or replacement. While the federal government reduced its taxes during the Reagan years by 7.6 percent, state and local governments have had to increase their revenue intake. State expenditures rose in the 1978-1987 period from $185 billion to over $250 billion. The bulk of the increases which provide infrastructure investment have come in the form of user fees and property tax increases. Earmarked or dedicated revenue sources also have become popular because voters can directly monitor the spending for programs of their choice. A recent National League of Cities study reveals that 67 percent of the cities polled had increased their user fees; 41 percent had increased their property taxes; 44 percent had decreased their capital spending; 25 percent had reduced their workforce; 22 percent had imposed hiring freezes; 14 percent had decreased services; and 8 percent had increased local income taxes.

Most states have not yet voted on their final budgets and tax increases this year. My research indicates, however, that only eight states are not going to raise taxes of any sort. Of the remaining forty-two states and the District of Columbia, sales and excise taxes are the likely targets for budget balancing increases. Thirty states are considering sales and excise tax increases. Twenty-three are considering what I would call user fee or service taxes. Nineteen are considering gas tax increases which also is being discussed as the source of a deficit reduction tax at the federal level. Nine states are considering individual income tax increases, while four are considering corporate tax increases. Obviously many states are considering tax increases in several categories in their efforts to balance their budgets.

I will submit for the record the list of states currently considering each type of tax increase so you may see for yourselves the variety of options being contemplated. Eighteen states plan to dedicate some of the tax increases directly to infrastucture programs. Eleven will dedicate part of their taxes for healthcare and other social programs.

Nevertheless inflation has outstripped the ability of these revenue sources to provide adequate infrastructure investment. While state and local governments continue to raise taxes, increasingly they are forced to rely upon tax-exempt borrowing to meet the investment short fall. Since the incessant search for federal revenues started by Gramm-Rudman, state and local governments have been treated like competitors for tax revenues, rather than partners sharing the costs of our mutual policy goals.

Abusive transactions like escrow deals concluded hurriedly to forestall the effects of tax reform and the Deerfield, Illinois transaction, where a small community borrowed far more than it needed in order to earn arbitrage, are glaring examples of why Congress felt justified in treating other levels of government like special interests. However the sensitivities of the municipal market and the need for private investment in public projects demand that the legislative response to apparent abuses should not be overkill. In other words, let's not go hunting for gnats with an elephant gun -- or a semi-automatic.

To the extent that the federal government can work with and be supportive of state and local governments, they will be far better able to assume responsibility for problems which mutually plague all levels of government. If local infrastructure investment helps boost the productivity of local businesses, and increased productivity means increased economic growth, and increased growth means increased federal revenues, then the interests of all parties to federalism are one and the same, not conflicting.

We in Congress need to acknowledge the idiosyncracies of public finance and must try to be more responsive to the concerns expressed by state and local officials. Constant changes in the tax rules have made public officials, who like members of congress have a public responsibility to represent and protect the interests of their constituents, believe that Congress just does not care about their local fiscal problems because the budget deficit looms so large. An acknowledgement by Congress that we are not going to dump our deficit problems on local government -- by taking away their ability to finance the solutions to these problems -- would help ease the tension which now exists. This tension or skepticism causes municipal and state officials to believe that if they do not borrow today for contemplated projects, Congress will have made matters worse by the time they are really ready to begin contstruction. The use of immediate effective dates by congress has raised their anxiety about our plans and caused rushes to market rather than stopping them.

Several years of tax law changes and concurrent legislatively spawned "abuses" are proof of this negative spiral of distrust. If Congress will use a scalpel instead of an ax when writing tax legislation, and if the practice of immediate or retroactive effective dates can be eliminated, "glasnoste" can begin. If we in congress acknowledge the increased costs to state and local governments and try to reduce that burden where we can, the public investment required to solve shared problems and to reach shared goals can go forward.

To address the ability of this Committee to help correct the balance in the current one-way system of federalism, I would commend to you that you review for yourselves the issues I have discussed today. If you concur with my view that the system has become imbalanced, with little federal support for the myriad of federal requirements, you should report your findings and share your conclusions with your colleagues. This would encourage the tax and budget committees to give more careful consideration to the combined impact of federal spending and tax policies on state and local government. Our policies should enable state and local governments to achieve the goal which we in Congress share with them: a sound and healthy foundation for America's communities.

Thank you for this opportunity to testify before your Committee. I will be sure to forward to you the results of the Anthony Commission report and would be pleased to discuss them with you at your convenience.

ANTHONY COMMISSION

State Tax Developments

USER FEES & SERVICE TAX	SALES & EXCISE TAX	GAS TAX	PERSONAL INCOME TAX
Alabama	Alaska	Alaska	Colorado
Arkansas	Connecticut	Arkansas	Louisiana
California	D.C.	California	Maine
D.C.	Georgia	Colorado	Missouri
Georgia	Idaho	Florida	Montana
Idaho	Illinois	Kansas	Nevada
Indiana	Florida	Louisiana	New Jersey
Iowa	Kansas	Maryland	Oklahoma
Kansas	Louisiana	Minnesota	Virginia
Louisiana	Massachusetts	New York	
Maryland	Michigan	North Carolina	
Michigan	Mississippi	North Dakota	
Missouri	Missouri	Oregon	
Nevada	Montana	Tennessee	
N.H.	Nevada	Virginia	
N.J.	N.H.	Washington	
N.Y.	N.Y.	W.VA.	
N.D.	N.C.	Wyoming	
Oregon	N.D.		
S.C.	Ohio		
S.D.	Oklahoma		
Washington	Oregon		
W.VA.	R.I.		
	S.C.		
	Tennessee		
	Texas		
	Virginia		
	Washington		
	W.VA.		
	Wyoming		

CORPORATE INCOME/ BUSINESS TAX
Nevada
N.H.
Washington
W.VA.

FRANCISCO L. BORGES
TREASURER

State of Connecticut
OFFICE OF THE TREASURER

EDWARD J. FORAND JR.
DEPUTY TREASURER

Testimony of Francisco L. Borges

Treasurer
State of Connecticut

to the

U.S. Senate Governmental Affairs Subcommittee
on General Services, Federalism, and the District of Columbia

in re

INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

Room 342
Dirksen Senate Office Building

May 4, 1989
10:00 a.m.

55 Elm Street   Hartford, Connecticut 06106-1773
An Equal Opportunity Employer

Good morning, ladies and gentlemen, esteemed colleagues, the Honorable Jim Sasser, chairman of this committee, Senator Joseph I. Lieberman, Senator Jeff Bingaman, Senator John Heinz, and Senator Ted Stevens.

I am Francisco L. Borges, Treasurer of the State of Connecticut. As such, it is I who am responsible for overseeing the bonding activity of the State of Connecticut, and it is in that capacity that I appear before you today to discuss the financial impact on the states of current federal policies affecting the preservation and maintenance of our state and national infrastructure.

You may be interested to know that the State Treasurer has been the chief fiscal officer of Connecticut since 1639 -- when Connecticut was still a colony. The Office of the State Treasurer is the financial cornerstone of state government in Connecticut, with authority to oversee a wide variety of activities having to do with the prudent management of state funds, including the administration of a multi-billion dollar investment portfolio of pension assets and the execution of a multi-million dollar bonding program.

In Connecticut, the Treasurer is one of six constitutional, popularly elected state officers. As directed by the state Constitution in Article Fourth, Section 22, he or she is responsible for receiving all monies belonging to the state, making disbursements as directed by statute, and managing, investing and borrowing all funds for the state.

As the Treasurer of a beautiful and much-blessed state -- but one that is experiencing its share of fiscal problems -- I very much appreciate having been given the opportunity to speak with you today on a matter of grave concern to all of us -- namely, our aged and ailing state and local infrastructures.

We all know that the stakes are high.

As Chairman Sasser so aptly noted in his kind letter of invitation to me, without an adequate infrastructure -- consisting of the three main components of transportation, water and solid waste disposal -- no economic activity is possible.

And, as he also noted, the degree to which economic activity is possible is directly linked to how adequately the infrastructure can sustain that activity.

We in Connecticut understand that relationship, and are in fact in the midst of an ambitious program whose purpose is to ensure that the state's infrastructure remains viable.

The main portion of our infrastructure renewal program in Connecticut so far has to do with the maintenance, rehabilitation and rebuilding of our roads and bridges.

But we in Connecticut are also concerned about the infrastructure in a larger sense -- encompassing not only streets and highways and bridges and culverts, but also water and sewerage systems, sidewalks and curbs, public buildings and public parks, dams and flood control facilities, solid and hazardous waste disposal, and air, rail, bus and water transportation facilities.

"Infrastructure" is an encompassing term, and it is also a relatively new term.

Yet from our earliest days on this planet, we humans have recognized the importance of an adequate, properly maintained and intelligently planned infrastructure. It is no accident that roads, walls, canals, aqueducts, boats, carts and yes, the wheel itself, are among the oldest objects crafted by human hands.

They are still among the most useful, whatever form they take. Besides allowing commerce to occur and flourish, an adequate infrastructure is essential to human communication, human health, and human happiness.

Thus, the infrastructure and the economic and human benefits it makes possible are part of a larger human ecology. Indeed, the origins of "economy" and "ecology" have the same root: "oikos" or "ecos", the ancient Greek word for "household."

Economy is the "nomos" or numerical side of our human household, while ecology may be said to be the inherent internal logic of our human systems.

Strangely enough, in today's society, economy and ecology have too often become alienated from one another -- although they should be and are cousin concepts that unite the human household.

What does this have to do with infrastructure problems and issues? Quite simply, we who are gathered here today have an opportunity to emphasize that the infrastructure, uniting economy and ecology as it does, must not be sacrificed or neglected for apparent short-term economic gain. Prudent investment in the infrastructure cannot be sacrificed however great our budget deficits. When bridges, streets and water pipes fall apart, the economy begins to fall apart.

It is by now a truism that, in general, the nation's infrastructure is, in the words of the National Council on Public Works Improvement, "barely adequate to fulfill current requirements, and insufficient to meet the demands of future economic growth and development."

The Council has estimated that on a national basis, the cost of meeting infrastructure needs this year is expected to be double the $45 billion that was spent in 1985 for new and upgraded infrastructure.

On the local and state levels, the costs are equally staggering.

Yet far from helping states meet the challenge of doing the financing they must to pay for maintenance and improvements to aging infrastructure, the federal government has made the challenge tremendously difficult, if not impossible, to meet.

The prime culprit is the administrative nightmare caused by certain requirements of the 1986 Tax Reform Act, about which I will say more later. Another culprit is the federal government's apparent intention of limiting local governments' access to the tax-exempt bond market.

I will explain in some detail in a moment, but first let me give you some background about the situation in my own state.

In my home state of Connecticut, not so long ago, we were given ample and tragic proof of just how inadequate our infrastructure was becoming -- how old, decrepit and neglected it was.

On the evening of June 28, 1983, a major bridge carrying a major section of the Connecticut Turnpike over the Mianus River in Greenwich suddenly and silently collapsed, without warning, causing three people to plunge to their deaths in the waters below.

It was a horrifying tragedy that awakened everyone in Connecticut to the fact that our roads, highways and bridges needed immediate attention.

The deaths of three innocent people were a grim and unwelcome reminder that Connecticut was reaping the whirlwind of years of neglect and deferred maintenance of our roads and bridges.

Fortunately, Connecticut's governor, William A. O'Neill, is a foresighted man. On April 12, 1983, he had announced -- even before the Mianus River Bridge tragedy -- that he was forming a special Governor's Task Force on Infrastructure.

The governor directed the Task Force, composed of members from state and local governments and the private sector, to develop a coordinated strategy for infrastructure improvements.

With the collapse of the Mianus River Bridge on June 28 of that year, Gov. O'Neill, to his everlasting credit, directed the Task Force to place special emphasis on infrastructure issues that directly affect the public safety.

Almost immediately, the state hired outside experts to assist in developing a financial plan to deal with highway and bridge repair. The Task Force also surveyed the condition of all public works, public buildings, roads, bridges, dams and other such structures, and began to study ways to repair them where needed and to pay for the repairs.

During a special legislative session that year, the governor proposed and the Connecticut General Assembly passed a $42 million package to repair the Mianus River Bridge; to fully fund the first year of an updated 10-year transportation plan, including funds for highway and bridge repair, to establish a new class of inspectors in the State Department of Public Safety to beef up the monitoring of overweight truck traffic on the Connecticut Turnpike and other major thoroughfares, and to provide the State Department of Transportation with more personnel and equipment for the maintenance and inspection of roads and bridges.

Ultimately, Gov. O'Neill proposed a comprehensive 10-year, $5.5 billion plan for complete overhaul of the state's infrastructure, saying that what he proposed was nothing less than a complete modernization of "the very lifelines of the Connecticut economy."

The governor made no bones about the fact that the program would cost dearly, including a significant increase in the gasoline tax, increases in driver's license and automobile registration fees and fines, and ambitious new dedicated bonding programs and creation of a special new dedicated transportation fund.

To their credit, the people of Connecticut accepted the plan instantly, understanding that the public safety and the continued vibrancy of the State's economy demanded it. Even the Senate Minority Leader, Philip S. Robertson of Cheshire, a gentleman from the opposite party, said the governor's plan "deserved accolades."

Among the highlights of Connecticut's 10-year plan -- now well underway -- are the following:

-- Resurfacing of 500 miles of roads each year.

-- Modernization of the entire highway system, using more than $2 billion in state and federal funds.

-- Reconstruction within three years of 520 state bridges rated in fair or poor condition, and the repair of another 110 bridges after that.

-- A $185 million program to provide grants and low-interest loans to cities and towns for bridge repairs.

-- Replacement of state-owned buses and the construction of new bus garages at a cost of $27 million.

-- Overhaul and replacement of commuter rail cars at a cost of $32 million.

-- Improvements at airports throughout the state, including a $100 million renovation and rehabilitation of Bradley International Airport in Windsor Locks, paid for by a separate dedicated bonding program costing $100 million.

Of the $5.5 billion total for the 10-year plan, we in state government set the state's share at $2.2 billion, with the rest to come from the federal government, based on the assumption that existing levels of federal funding would continue.

We anticipated that of total costs over 10 years,

-- 52 per cent would come from the federal government
-- 37 per cent would come from the sale of special transportation obligation bonds
-- 8 per cent would come from appropriations, and
-- 2 per cent would come from other sources, such as matches from local governments, developers' assessments for project benefits, etc.

So far, through April 1 of this year, Connecticut has spent $1.473 billion against transportation infrastructure renewal.

Naturally, it would be far easier on us if the federal share of funding for this project were at, say, the 75 per cent level.

Obviously, every state would like more federal dollars for its infrastructure needs, and Connecticut is no exception.

And it is important to bear in mind that with fees, user fees and resources like gasoline taxes, transportation is perhaps the easiest portion of the infrastructure to fund. Asbestos removal, renovation of public buildings, and water and sewer projects are all far more difficult to find money for.

What have we done so far with all these funds? We have made good progress, particularly in the road resurfacing and bridge rehabilitation program. To date:

-- 2,393.94 miles of two-lane roads have been resurfaced;

-- 546.27 miles of two-lane roads are to be resurfaced this year;

-- 687 bridges have been rehabilitated; and

-- 350 more bridges will be repaired this year.

I have gone into some detail in describing our infrastructure renewal plan to you, so show you the depth of commitment of one state -- and the staggering costs of that commitment.

Meanwhile, a full decade of federal retrenchment has sorely aggravated the fiscal burden our state bears in paying for other programs and services, including social ones. Like most other states with older cities, Connecticut has to find the money to pay for programs to address pressing social problems, even while we have to find the funds for infrastructure improvements and other major budget items like education.

While we have made good progress in repairing and refurbishing our roads and bridges, and have made an ambitious start in other areas, we in Connecticut have not yet done nearly enough on projects involving the other portions of the infrastructure that I mentioned before -- namely, water and sewerage systems, sidewalks and curbs, public buildings and public parks, dams and flood control facilities, solid and hazardous waste disposal, and air, rail, bus and water transportation facilities.

Here again, federal retrenchment has hurt us. Everyone knows that polluted waters have to be cleansed, that the environment must be purged of the toxic and hazardous waste oozing into the ground and the water and escaping into the air, yet the federal dollars just haven't been there for the states in sufficient amounts.

In his letter to me, Senator Sasser asked for detailed information as to future infrastructure costs, the impact of regulation and tax policy, including the effects of the 1986 Tax Reform Act.

I would now like to turn my remarks to those questions.

Future Infrastructure Costs:

Connecticut, my home state, is a fairly small, compact and relatively wealthy state, as states go. Yet, as I have indicated, the costs of restoring and extending our infrastructure have been -- and will be -- enormous.

Our ten-year program, now underway, was originally set at $5.5 billion; its cost has risen with time and inflation to $6.68 billion. A statewide billion-dollar pollution control effort is also underway. A half-billion dollar program to relieve prison overcrowding has also begun.

And hundreds of millions more are being spent in Connecticut on local infrastructure projects, public schools, public buildings, colleges and universities and on housing and economic development programs.

Meanwhile, the state's share of the transportation infrastructure renewal program has grown to $3.1 billion, financed by a dedicated fund that receives all gasoline tax revenues, motor vehicle fines and motor vehicle fees. The fund pays the debt service on special tax obligation bonds that are issued to finance the construction projects.

The other programs I mentioned are funded by ordinary general obligation bonds. There are no gimmicks or shortcuts, because as you are well aware, construction projects on that scale require cash in large quantities.

Connecticut's capital budget has grown to -- and through -- the billion-dollar per year mark. This scale of investment cannot be sustained indefinitely by a state as small as Connecticut. The situation is aggravated by the fact that local capital investment needs are equally great.

Impact of Federal Regulation and Tax Policy:

Except in the area of transportation, where the federal government has continued to act as our partner, and in the area of pollution control, where federal contributions are helping to capitalize state pollution control revolving funds, the primary federal role in state and local infrastructure renewal has been one of abdication and complication.

The federal government has walked away from housing assistance, from community development projects, and from economic development. No real assistance is available for prisons, school construction, university construction or the construction or renovation of public buildings.

Senator Sasser also asked me to discuss whether state governments will be able to meet the financial requirements of maintaining and developing needed infrastructure improvements, and to discuss the financing techniques that are being used. I was also asked whether new rules and regulations have made the initiation and management of tax-exempt bond issues simpler or more difficult for state and local governments.

The simple answer, in plain unvarnished English, is this: States cannot meet the challenge by themselves, and, in Connecticut at least, as a result of so-called "tax reform," we have had to go through prolonged, expensive and totally unnecessary financial contortions to try to finance projects at all.

Specifically, the problems created by the federal government in recent years are as follows:

1. The states' need to comply with the requirements of the federal Tax Reform Act of 1986 has created a hugely unproductive administrative tangle.

The State of Connecticut alone must spend well in excess of $1 million per year to collect data on -- and have bond and tax counsel analyze -- each of the thousands of projects paid for by our general obligation bond issues.

When we use bonding to raise funds to pass through to local municipalities, the arbitrage requirements of the 1986 Act are nearly beyond belief. Unless all such pass-through funds are invested in tax-exempt securities that are not subject to the alternative minimum tax, we must track expenditure and investment earnings on those funds until the ultimate recipient has fully expended them.

Such tracking for the more than 1,000 projects currently in progress would be absurdly expensive.

In order to cope with the 1986 Act, we in Connecticut instead have set up a special Tax-Exempt Proceeds Fund, with appropriate safeguards on deposit and expenditure, in order to keep the pass-through money flowing.

While I am proud that Connecticut is the first state to set up such a fund, its set-up and operation has been an expensive and labor-intensive process with absolutely no reason to exist other than to meet the federal arbitrage requirements of the 1986 Tax Act.

2. The requirements that apply to the Clean Water Fund and to other pooled and revolving loan programs add more major expense and more difficulties.

Most orderly construction assistance programs advance money as work progresses. The pooled loan requirements imposed on us demand that we advance all of the money raised through bond proceeds within six months, or that the bond proceeds be yield-restricted.

The yield restriction requirements are cumbersome and expensive to administer. The arbitrage provisions relative to revolving loan funds require that every dollar be traceable back to the original bond issue, so that each time it revolves back to the fund an arbitrage calculation can be made. The alternative -- yield restriction -- erodes the value of the fund to absolutely no one's benefit.

3. While the federal government has walked away from housing assistance and has greatly reduced economic development assistance, the Unified Volume Cap on so-called "private activity bonds" and other limitations on bond issuance for those purposes have severely limited the ability of states and cities to fill the void.

Connecticut has had to issue taxable general obligation bonds in large volume to maintain housing and economic development programs entirely on its own.

So, in general, at a time when infrastructure development and renewal needs are growing, the federal government has not only reduced the assistance it provides in those areas, but has also added mightily to the costs and complexity of state and local efforts to meet their own needs.

To respond to another of Senator Sasser's questions, in my view it is fruitless and wrong-headed to look to the private sector for significant relief. Certainly private industry has a role to play -- and a stake in -- making our communities better places to live and work, including helping with infrastructure improvements where possible and feasible.

In the city of Raleigh, North Carolina, for example, real-estate developers as I understand it agreed to pay sewer hookup fees in advance of construction, thus financing one-third of the cost of building 17 miles of new sewer lines and a pumping station. Some cities have experimented with so-called "linkage fees" that try to tie downtown development with neighborhood revitalization, including local road and economic development projects.

But these are not real solutions. The prime responsibility for maintenance of the infrastructure -- because at bottom it affects the public health and safety -- must rest with government. And state and local governments, increasingly, are in serious need of federal help.

In order to provide the services that the public requires and deserves, state and municipalities must for one thing continue to be permitted access to the tax-exempt bond market.

Over the past two years, that access has been ravaged by a series of legislative actions that -- in the name of revenue generation, or in the alleged interest of ending so-called "abuses" -- have imposed a burden on states and municipalities that far exceed any benefits to the federal government.

Moreover, this spring the U.S. Supreme Court overturned a 100-year precedent in South Carolina v. Baker, by saying that the issuance of tax-exempt debt was no longer constitutionally guaranteed. This attack on the long-standing notion of intergovernmental tax immunity -- one of the pillars of our federalist system -- has left states and municipalities at the mercy of further deleterious cutbacks by Congress.

I strongly urge this committee and the tax-writing committees of Congress to become more familiar with the considerable problems created by these legislative and judicial trends and to make preservation of the tax-exempt bond market a major priority.

Over the years, tax-exempt bonds have become an essential financing mechanism for infrastructure projects such as the construction of schools, public buildings, transportation systems, water and sewer systems and others.

Congress and the present administration have the authority and the opportunity to dictate the future of public finance. This must include setting an agenda for legislation (tax-regulated or otherwise) having to do with bonds, helping to guide the promulgation of Treasury regulations dealing with bonds, and, in general, defining a national policy that emphasizes the importance of tax-exempt financing in meeting state and local infrastructure needs.

I am directing my comments to you today not only in my capacity as State Treasurer of Connecticut, but also as an officer of the National Association of State Treasurers, an organization of state financial officers which has endorsed the points I am making.

Both the association and I invite and encourage this committee, and any others in Congress, to work with us as State Treasurers to develop new policies or procedures affecting our ability to issue bonds and otherwise manage public debt and financing.

Only such a cooperative effort will ensure sound policies that more fairly balance the needs of state and local governments with the needs of the federal government.

Once again, I appreciate having had the opportunity to appear before you today, and I welcome your comments or questions at any time.

Thank you very much.

QUESTIONS FOR TREASURER BORGES REGARDING THE EFFECTS OF THE TAX REFORM ACT OF 1986 ON INFRASTRUCTURE FINANCE

Arbitrage Requirements

Question: Prior to the 1986 Tax Act, how big a role did arbitrage profits play in state infrastructure financing? Typically, what percentage of the cost of the public works projects in Connecticut was offset by arbitrage profits?

Answer: Arbitrage profits have never played any meaningful role in Connecticut's infrastructure financing. Our debt issuance was timed to the cash flow needs of all of our capital projects taken together. The proceeds of each bond issue would, in an accounting sense, be credited to the projects in specific bond fund accounts, but the cash was available through our common cash pool for any capital projects. It was very rare that any bond proceeds would remain unspent more than a few months after the date of issuance. Proceeds were, therefore, invested only in short term investments which provided daily liquidity and ready access. In a normal market, our average long-term, tax-exempt interest rate and the short-term taxable rate received on invested proceeds is about equal. Arbitrage earnings were never a material factor in our infrastructure financing.

It is also one of the ironies of the Tax Reform Act that we can no longer use the fungible cash pool approach without potentially running afoul of arbitrage tracking requirements. This limit on our ability to flow cash from where it is to where it is needed, has required that we accelerate our bond issuance program to assure that funds are available within each capital project account as needed. As a result, the average length of time from issuance to expenditure of each dollar has about doubled.

Question: What has been the cost to Connecticut of compliance with the arbitrage requirements? Have you had to hire outside firms to comply with arbitrage tracking requirements? At what cost?

Answer: Thus far, the direct cost of compliance with arbitrage requirements has not been very burdensome. We have set up spreadsheet programs to track actual invested balances at actual rates of interest versus the interest rate on the bonds. Annually, we compute the actual arbitrage earnings and set this amount aside in an interest bearing account for future rebate. All of this requires about half of one accountant's time to maintain this approach. We have had to consult with bond and tax counsels on various compliance issues, but have not had to retain other outside help.

The newly-issued arbitrage regulations may change this significantly. It appears that we will not be permitted to track actual earnings in the relatively simple way we are doing so, but will be required to do potentially complex future value calculations which are supposed to approximate actual. It is an open question whether we will purchase software to do this internally or will have to contract it out.

There are also some major indirect costs to arbitrage tracking. The State of Connecticut capitalizes a variety of relatively small revolving loan funds for local governments and non-profit groups. Many of these capitalization grants could theoretically be funded with tax-exempt bonds, but the arbitrage requirements for revolving funds are complex beyond belief. Taxable bonds are, therefore, issued. Another range of indirect costs is described in the answer to the next question.

Question: Could you provide some additional information on the Tax-Exempt Proceeds Fund, which you mentioned in your written testimony. Is the main purpose of the fund to insure that arbitrage profits are spent within the 6-month time limit?

Answer: The State of Connecticut passes through in the form of grants or loans over $100 million a year in tax-exempt bond proceeds to municipalities and non-profit organizations for a variety of infrastructure purposes. Such proceeds are not "expended" for arbitrage purposes until the recipient organization spends them. Unless those proceeds are invested in tax-exempt securities, we are responsible for tracking, documenting and rebating any arbitrage investment resulting from their investment of the funds. Such tracking for hundreds of recipients and thousands of projects cannot be done with sufficient reliability to permit us to issue tax-exempt bonds. The Tax-Exempt Proceeds Fund (TEPF) was established as our only feasible alternative to permit the pass-through programs to continue. A copy of the fund's prospectus, the administrative procedure which state agencies must follow to assure that money which must go into the fund does go into the fund and a list of account holders are attached.

The TEPF is a costly operation which has no reason to exist, but for the Tax Reform act of 1986. Direct operational costs amount to 40 basis points. State agency administrative costs are considerable, but not dimensionable. Also, since the TEPF must be invested in very short-term tax-exempt securities, there is in a normal market about 100 basis points in negative arbitrage.

Question: Would Virginia Rutledge's suggested solutions solve the problem?

Answer: Yes, it appears they would. Another potential approach is to exempt any state or municipal general obligations bond to which the issuing jurisdiction has pledged its full faith and credit.

General Questions

Question: What percentage of the funds that Connecticut spends on infrastructure projects is raised through tax-exempt financing? What was the percentage before the 1986 tax changes?

Answer: Prior to the 1986 act, all infrastructure projects, with the exception of some highway resurfacing, were financed with tax-exempt bonds. Now, about 10% of the projects require taxable bonds.

Question: Can you estimate the overall increase in the cost of public financing as a result of the changes in the 1986 tax act?

Answer: For the State itself and the recipients of its tax-exempt bond proceeds the costs are roughly as follows:

1. Added State-agency staff time to collect all of the data required for "private activity" analysis - about $500,000 per year.
2. Added legal fees - primarily for "private activity" analysis - about $1,000,000 per year
3. Systems development and programming to accommodate added information which must be stored and tracked - $3.5 million
4. Negative arbitrage resulting from the Tax-Exempt Proceeds Fund - $300,000 per year
5. Cost of operating the TEPF - $200,000 per year
6. Arbitrage tracking and extra staff due to the new complexity of bond issues - $100,000 per year

Connecticut has also decided to continue its policy of financing needed statewide economic development and housing programs, even though it has meant issuing taxable general obligation bonds. This has resulted in significantly higher issuance costs, including the cost of borrowing. It is expected that the state will spend between $15 and $20 million per year in extra interest costs over the 20 year life of all its taxable bonds.

Question: Is there a particular area of publicly financed activity which has been hardest hit?

Answer: The administrative burdens have affected all activities, but housing has been affected the most overall. The "private activity" analysis has been the most expensive and intricate. this area has also required the highest proportion of taxable bonding. Virtually all of it involves pass-throughs with their special problems. Many revolving funds are also involved.

Question: Is there some lesser step other than a constitutional amendment which Congress could take?

Answer: Federal securities are unconditionally exempt from state taxes without any qualification procedures. The revenue loss to states is in the billions. Congressional actions have repeatedly labelled and treated state and municipal governments which are seeking to meet their infrastructure needs as "special interests." Fairness suggests reciprocal immunity. That could be statutory rather than constitutional. Experience of recent years, however, leaves state and local governments with limited faith in fair statutory solutions.

UNITED STATES SENATE

COMMITTEE ON GOVERNMENTAL AFFAIRS
SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM
AND THE DISTRICT OF COLUMBIA

HEARING ON

INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

May 4, 1989
Washington, D.C.

Statement by

Howard Yerusalim, P.E., Secretary
Pennsylvania Department of Transportation
1200 Transportation and Safety Building
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Mr. Chairman and distinguished members of the Subcommittee, I am Howard Yerusalim, Secretary of Transportation for the Commonwealth of Pennsylvania. I am pleased to be here today to share my views on infrastructure problems and intergovernmental solutions.

The term "infrastructure" is broadly defined as the underlying foundation or basic framework of a system or organization. Being from the transportation community, I will focus my statement on transportation infrastructure--the nation's vast network of highways and bridges, transit systems, railroads, airports and ports and waterways.

Transportation infrastructure is widely recognized as a major component of the nation's system of public facilities. The condition and performance of transportation systems is directly linked to economic development and to national and international competitiveness, since the ability to move people, goods and services quickly and cost-effectively is key to economic health and vitality in today's fast-paced world.

But our transportation infrastructure cannot be taken for granted; it needs constant attention. Consider, for example, the Interstate Highway System, a hallmark of public works endeavors representing an investment of well over $100 billion nationwide over the past three decades. Already, many segments of this modern highway network have exceeded or are nearing their design life and require major rehabilitation or reconstruction. In Pennsylvania, we spend more than $100 million per year to restore and preserve our Interstate System. The total transportation budget at the state level in Pennsylvania is expected to be approximately $3.3 billion for fiscal year 1989-90, a substantial investment in transportation infrastructure and services.

Given the critical importance of transportation infrastructure to this nation and its economy, it is absolutely essential to have program and institutional structures in place which facilitate the delivery of safe, reliable and cost-effective transportation facilities and services. Your invitation to me to participate in this hearing contained questions on specific aspects of program and institutional structures, and I will now respond to these in the context of my experience as a state transportation official.

FEDERAL, STATE AND LOCAL ROLES

What should be the roles of local, state and federal governments in planning, building, maintaining and financing infrastructure?

In general, there is an appropriate role for each level of government in planning, building, maintaining and financing transportation infrastructure. These roles are changing, and change is appropriate, I believe. However, the overriding principle which has guided transportation programs over the past seventy-plus years has been a strong federal/state/local partnership, a relationship which must be nurtured and must continue to evolve as circumstances change.

The major change I see occurring is that the states are becoming more capable of managing transportation programs and are assuming a larger role. Increasingly, the states are recognizing that the answer to transportation infrastructure challenges doesn't always have to involve a new federal program, and they are demonstrating the ability to successfully launch major transportation initiatives on their own.

For example, in Pennsylvania, we have a bridge replacement and rehabilitation initiative which we call the Billion Dollar Bridge Program. The program took its name from state legislation passed in 1982, which authorized work on approximately 1,000 bridges at an estimated cost of $1.4 billion. Since then, two more bills have been enacted, increasing the total amount of work authorized to $3.6 billion and the total number of bridges to more than 5,000.

The Billion Dollar Bridge Program has been very successful--to date, more than 1,000 bridges have been replaced or rehabilitated at a total construction cost of nearly $1.2 billion. The key to this success is a dedicated source of state revenue, raised through truck registration fees and a motor carrier road tax. The revenue from these sources totals more than $72 million per year, which, when combined with federal and local funds, enables us to undertake a bridge program totaling approximately $200 million per year. But most importantly, the improvements being made to Pennsylvania's bridges under the Billion Dollar Bridge Program are eliminating bridge weight limitations and bridge closings which impede truck traffic. Removing these impediments benefits intrastate and interstate commerce and has a positive ripple effect throughout the economy.

As we approach the 21st century, much attention is being given to the appropriate roles of the federal, state and local governments in transportation programs and financing. The American Association of State Highway and Transportation Officials, in which I am an active participant, is working with other transportation interest groups to identify consensus recommendations for future transportation programs and policies. Overall, I envision a federal role which is reduced in scope, but much more sharply focused on transportation issues and systems of national significance. This would leave an even larger role for state and local governments.

Even now, in specific instances, we see federal roles and philosophies changing, as evidenced by the gradual reduction in the federal presence in the transit and rail modes. However, in my view, this change is not taking place in an orderly fashion, and it seriously threatens the traditional federal/state/local partnership. As governmental roles are reshaped, it is important that there be a national transportation policy to set the tone, so that each level of government recognizes and willingly assumes its proper role. Without this framework, there will likely be an atmosphere of uncertainty and lack of direction, and the transportation infrastructure requirements of this nation will not be addressed in an effective manner.

To illustrate the changing federal role, consider that federal transit funding is on the decline, and there appears to be at least some sentiment for further cuts. Federal capital and operating assistance for Pennsylvania transit systems has been reduced from $379 million in 1980-81 to $155 million in 1987-88, a drop of nearly 60 percent. Federal funding for rail branchline improvements has been eliminated in the current fiscal year. Amtrak's appropriation has been set at a level which precludes a meaningful capital improvement program and threatens further service reductions. While these realignments of federal spending priorities may be appropriate for many reasons, it appears that they have been motivated by budget considerations rather than by any national transportation infrastructure strategy. In turn, this has placed increased pressure on state and local governments to provide financing.

Nearly $5 billion in public transportation capital investment requirements have been identified for the metropolitan Philadelphia region of the Commonwealth. This region is served by the Southeastern Pennsylvania Transportation Authority (SEPTA), the state's largest public transportation agency and the fourth largest in the nation. Even though state funding for SEPTA's operations has nearly tripled over the past decade (from $76 million in 1979-80 to $208 million in 1989-90), federal operating subsidies have declined by more than 50 percent over the same period (from $64 million in 1979-80 to $27 million in 1989-90), while local funding has grown at a steady rate (from $31 million in 1979-80 to $53 million in 1989-90). Meanwhile, over the last eight years, federal funding for annual transit capital improvement programs in southeastern Pennsylvania has been as high as $172 million, but the low mark for the period of $91 million was reached in the most recent year, 1987-88.

Given this situation, it will be extremely difficult to finance needed transit capital improvements in southeastern Pennsylvania from current federal, state and local sources. This situation is not unique to Pennsylvania, and underscores the critical importance of maintaining a strong federal role in the transit mode. Moreover, with a current balance of more than $5 billion in the Mass Transit Account of the Federal Highway Trust Fund--representing user taxes and fees collected for and dedicated to transit purposes--it is clear that the federal government could play a larger financial role in the federal/state/local transit partnership.

To summarize, the transportation infrastructure roles of the various levels of government are changing, but a national transportation policy is urgently needed to focus these roles and to ensure that program and institutional structures are in place not only to preserve these valuable transportation assets, but also to enhance them.

Under current policies, do you have the capacity to meet these responsibilities?

Assuming that this question is addressing current federal policies, I would refer to some of the difficulties mentioned previously with respect to the changing roles of the various levels of government in transportation infrastructure. Overall, though, the answer to the question is "yes," I have the capacity to meet my responsibilities as a state transportation official under current federal policies.

From an operational standpoint, federal transportation programs have evolved under a partnership concept, and the policies which guide these programs enable them, for the most part, to function effectively in tandem with state and local programs. I would point out, however, that the trend toward greater state and local roles in transportation requires that current policies be re-examined and restructured to allow a greater degree of flexibility.

Which policies work well and what changes would you recommend?

Overall, the federal transportation policy which has served the nation best is that of a federal/state/local partnership based on the principle of dedicated user financing for federally-supported programs, with project selection left to state and local officials.

In general, the federal program policies which have worked well are those that represent a firm commitment to a national objective. The Interstate Highway System is a prime example. Construction of this System has dominated the federal-aid highway program for more than thirty years, and the states have proceeded to construct the System over this period with the assurance of full federal funding to complete it. The System is nearly finished, and the federal commitment to complete it must be kept, which, according to the latest cost estimates, means that $3 billion in additional federal fund authorizations must be provided. This is especially critical for Pennsylvania and other states which have utilized "advance construction" provisions to place Interstate projects under construction before sufficient federal funds were actually apportioned to them, and, in effect, are pledging state funds to cover the federal share of the costs of these projects until the federal funds become available.

Pennsylvania and a number of other states are now constructing the final links of the Interstate System. The construction of the Interstate System has been a success because there has been a strong and unwavering commitment at the federal and state levels to build a "national" highway system. Although there have been numerous program proposals for the "post-Interstate era," I am concerned that there is no similar level of national commitment to transportation infrastructure in place for the future.

In terms of changes I would recommend, the most basic would be to allow more flexibility in federal transportation programs. This call for greater flexibility covers a wide range--from relaxation of design requirements, to increased transferability among federal fund categories, to the elimination of sanctions, to broadening the applicability of toll financing, to name only a few. Such increased flexibility is especially important in view of the trend toward greater state and local government roles in transportation infrastructure programs.

I would also like to see a more needs-based allocation of federal funds among the states. I mentioned previously the large requirements in Pennsylvania to preserve our Interstate Highways. However, the present apportionment formula for federal Interstate Restoration funds is based on Interstate lane-miles and vehicle miles of travel, and does not take into account the effects of heavy truck traffic which occasion a large portion of the pavement restoration requirements on the Interstate System. As a result, Pennsylvania, which is the crossroads for interstate commerce in the Northeast, has had to spend state maintenance funds to restore and preserve its Interstate Highways, since only about $100 million per year in regular apportionments and discretionary allocations is made available to us for this purpose through the federal-aid highway program.

Finally, I endorse measures that reward states for taking infrastructure improvement initiatives which are not required by federal law. Pennsylvania's Billion Dollar Bridge Program is an excellent example, and I applaud Senator Heinz for introducing a bill which would increase the overall funding for the federal bridge program and would direct additional funds to those states which have attempted to help themselves at the state and local levels.

ROLE OF THE PRIVATE SECTOR

What should the role of users and private developers be in financing infrastructure improvements?

Dedicated user financing has been the hallmark of transportation programs over the years, and this proven method should continue to be the basic source of funding in the future. Since the benefits of transportation facilities and services accrue primarily to users, the user financing concept has worked well and is widely accepted. Even so, there are equity issues in the user financing structure which must be examined, including the imposition of taxes and fees which result in fair share payments by all users under cost allocation principles. Also, in the interest of equity, I believe that certain federal tax and fee exemptions (such as the present exemption of gasohol from a portion of the federal fuel tax) should be eliminated and that every effort must be made to reduce tax and fee evasion. Overall though, it has been shown repeatedly than users of transportation systems are willing to pay for the maintenance and improvement of the transportation infrastructure which serves them.

However, it is very important that the present dedication of these user revenues to transportation purposes be continued, and that all transportation user revenues be made available for expenditure for the purposes for which they were collected. I oppose the present practice of holding large balances in federal transportation trust funds to offset deficit spending in other elements of the federal budget. For example, at the beginning of the current federal fiscal year, the combined balance in the Highway and Mass Transit Accounts of the Federal Highway Trust Fund totaled nearly $14.2 billion, and the balance is expected to increase to more than $15.7 billion by the end of this fiscal year. I also oppose any increase in the federal motor fuel tax for deficit reduction purposes and any use of fuel tax revenues for non-transportation purposes. Although reducing the federal budget deficit is a clear national priority, the importance of transportation infrastructure to the nation's well-being is also very clear.

While all indicators point to user taxes and fees as the mainstay of transportation finance, the role of private developers in funding infrastructure improvements is growing, and appropriately so. In theory, the private developer should be responsible for all of the costs of improving the transportation system to serve the additional requirements generated by his development. In practice, a broad range of cost-sharing arrangements is possible, based on state and/or local policies and ordinances, evaluations of benefits accruing to the various users of the transportation system, and other considerations such as right-of-way donations. The use of financing methods such as local options taxes and private developer contributions must increase if we are to effectively address transportation improvement requirements.

What are the possible negative impacts of private participation on infrastructure public policy decisions?

In my opinion, the most serious possible negative impact is the perception that undue preferential treatment or special priority is being given to projects which involve private participation. This is an important issue in instances where a project requires a combination of public and private financing. Care must be taken to avoid tilting the balance of public funding inappropriately toward growth areas at the expense of non-growth areas.

In Pennsylvania, we have a formal transportation partnership process established by a state Transportation Partnership Act, whereby private interests can work with local governments to finance improvements to the transportation system. However, our policies clearly state that partnership projects will be evaluated along with all other projects eligible for public funds, and that these projects must compete for inclusion on the Commonwealth's Twelve Year Transportation Program as a condition for any federal or state fund participation.

IMPROVED INTERGOVERNMENTAL COOPERATION

What steps should be taken to improve intergovernmental and public/private partnerships to promote more efficient management of resources (e.g., communications, conflict resolution, technology transfer)?

As mentioned previously, I believe that the key to improved intergovernmental and public/private cooperation is the clear definition of roles based on an agreed-upon set of transportation infrastructure policies and strategies. Beyond that, there must be structured processes (either legislated or administratively implemented) which involve all parties as partners in decision-making. If there is a "buy in" on the policies, strategies and processes, the difficult tasks of communication, conflict resolution and technology transfer are made much easier.

From my perspective as a state transportation official, there is good cooperation overall between federal and state transportation agencies, even though present institutional and program structures do not always lend themselves to a cooperative approach on multi-modal issues. My experience with the Federal Highway Administration has been especially good--we have a very positive working relationship.

In my view, intergovernmental and public/private cooperation can only become more important in the future as we strive to work together to address the difficult mobility issues which face transportation decision-makers. As urban and suburban congestion becomes an even more pressing issue, it becomes clearer that highway solutions are not the only alternative. A full range of options, including transit expansion and transportation demand management, must be carefully examined and evaluated. This suggests that some of the existing program and institutional barriers to intergovernmental cooperation must be penetrated if we are to have meaningful ways to bring all available resources to bear on the most critical mobility and transportation infrastructure issues. Moreover, environmental issues are becoming increasingly delicate, which again signals the need to work cooperatively through structured, participative processes.

Can you give examples of projects which have worked well in the Commonwealth?

Improving the interchange between US Route 202 and PA Route 29 in Chester County (suburban Philadelphia) was the first application of Pennsylvania's Transportation Partnership Act. In this instance, two township governments worked with the local business community to identify transportation improvements needed to handle increased traffic occasioned by the location of high-tech firms in the vicinity of the interchange. A transportation authority was created under the provisions of the Act, with the authority to assess business property. The authority issued bonds to raise the local funds, which will be paid off with the proceeds of the assessments. The project itself involves widening of Route 29 and major improvements to the interchange to improve access to the Great Valley Corporate Center. The first phase of the project, costing $3.5 million, was completed by the area's largest developer. The second phase, which will be underway shortly at an estimated cost of $20 million, is being funded by the Commonwealth and the authority.

In addition to formal arrangements under the provisions of Pennsylvania's Transportation Partnership Act, we are also involved in informal partnerships related to specific transportation improvements. One example involves the new site of the Ford Electronics and Refrigeration Corporation in Montgomery County. The new facility will generate traffic which will impact conditions on area roadways and intersections. A $2.7 million program of projects has been identified to address these impacts. A cost-sharing arrangement has been agreed to, whereby the corporation will contribute $623,000 toward the improvements and will work with us to ensure that the local transportation system functions effectively. Instances such as these demonstrate the willingness of major corporations (Ford Electronics and Refrigeration contributes more than $1 billion annually to Pennsylvania's economy) to work cooperatively to address specific transportation requirements.

Another example of a formal transportation partnership in Pennsylvania is the Thorn Run Interchange on the Parkway West in Moon Township, Allegheny County, near the Greater Pittsburgh International Airport. This $6 million project, scheduled to go to construction this year, will replace an inadequate at-grade intersection. Funding for the project includes $3 million from the state, $1 million from the Department of Defense and $2 million from the Moon Township Authority. The Authority has issued bonds, which will be retired with proceeds of taxes on new development and assessments on landowners. It is estimated that this project will lead to 7,600 new jobs by the year 2000. Recently, the Federal Highway Administration presented an innovative financing award to the Moon Township Authority and the Pennsylvania Department of Transportation to recognize the creativity shown on this project.

The final project I will discuss is the Midfield Terminal/ Southern Expressway. This is a major project to improve land and air travel in Southwestern Pennsylvania. The new Midfield Terminal complex is under construction at the Greater Pittsburgh International Airport. It will consist of airside and landside terminals connected by an underground automated people mover. The $567 million project is being financed with federal, state and local funds and by the air carriers. Employment at the airport is expected to increase by 10,000 as a result of this new facility, and development on adjacent land is expected to add another 4,000 jobs. The terminal is expected to be completed by late 1992.

A proposed Southern Expressway is being planned to provide the necessary access to the Midfield Terminal and to open up several thousand acres of airport and private land for development. Construction of this multi-lane freeway is expected to begin in early 1990, with project completion scheduled to coincide with the opening of the new terminal. A steering committee has been formed to direct the development of the Southern Expressway to ensure that the objective of completing the highway by the time the terminal is completed is met. The steering committee includes representatives of federal, state and local agencies. The complexity of the environmental issues related to the project necessitated the formation of a special task force to coordinate preparation of the Final Environmental Impact Statement. The goal of the Task Force was to work cooperatively with the six federal and state environmental resource agencies to address the environmental issues, which include wetlands mitigation and hazardous waste disposal. Through the diligent efforts of the Task Force and the resource agencies, an agreement was reached to shift the roadway alignment to reduce wetland impacts, and concurrence was received from all parties in mid-April. This positive solution is very important to keeping the project on schedule, and I commend the cooperative attitudes of the six resource agencies--at the state level, the Department of Environmental Resources, the Fish Commission and the Game Commission; and at the federal level, the Environmental Protection Agency, the Fish and Wildlife Agency and the Corps of Engineers.

These are a few of the more prominent examples of effective intergovernmental and public/private cooperation in addressing transportation infrastructure improvement requirements that I would cite from Pennsylvania's recent experience. I would stress, however, that this approach of working cooperatively together is not just nice to have--it is absolutely essential for dealing with today's complex transportation infrastructure issues.

This concludes my statement, Mr. Chairman. Thank you for the opportunity to appear before this Subcommittee. I would be pleased to respond to any questions you may have.

Question Posed by Senator Lieberman

A recent article in the Washington Post estimated that a third of the nation's highway engineers will retire by 1995 without adequate replacements available. "In the next six years, state highway agencies will need to hire an average of 1,580 engineers a year," at a time "when engineering enrollments are steadily dropping. . . . " Do you anticipate this being (a) problem in Pennsylvania? Is your state considering ways to attract students to this field?

Response by Howard Yerusalim, Secretary of Transportation, Commonwealth of Pennsylvania

Yes, Pennsylvania is one of many states that is faced with the prospect of a shortage of available highway (civil) engineers and other transportation professionals.

The situation is exacerbated by the fact that many experienced engineers are reaching retirement age at a time when the need for such talent is generally on the upturn, but the number of students graduating from engineering schools is declining. We are stepping up our recruitment efforts in Pennsylvania accordingly, but this critical issue also requires and is receiving attention at the national level.

The American Association of State Highway and Transportation Officials (AASHTO), which represents the highway and transportation departments of the fifty states, the District of Columbia and Puerto Rico, has identified the development of transportation careers as an "emphasis area." AASHTO recognizes that the future of its member departments depends on attracting well-qualified candidates to enter careers in transportation.

AASHTO has appointed a Task Force on Transportation Professionals Development and Recruitment to prepare a plan of action to improve the overall supply and quality of transportation professionals. One of my Deputy Secretaries is serving on the Task Force. The work of the Task Force is in the early stages, but I understand that the products being considered include a guide for developing and refining a recruitment and retention program, and implementation of an aggressive "marketing" program aimed at cultivating early interest in transportation careers. The Task Force is planning to have these and other products available within the next year or two.

It is encouraging to see that there is growing recognition of the shortage of transportation professionals and of the problems which this shortage could cause. This gives me cause to be confident that by working together at the national, state and local levels, we can address this issue effectively and find positive solutions.

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STATEMENT OF

THE HONORABLE BURTON STALLWOOD

TOWN ADMINISTRATOR, LINCOLN, RHODE ISLAND

on behalf of

THE NATIONAL LEAGUE OF CITIES

on

INFRASTRUCTURE PROBLEMS & INTERGOVERNMENTAL SOLUTIONS

before the

SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM
AND THE DISTRICT OF COLUMBIA

COMMITTEE ON GOVERNMENTAL AFFAIRS

UNITED STATES SENATE

May 4, 1989

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Mr. Chairman, members of the committee: I am Burt Stallwood, Town Administrator of Lincoln, Rhode Island and Chairman of the Energy, Environment and Natural Resources Committee of the National League of Cities. I am also currently serving on the Office of Technology Assessment's advisory board on an ongoing infrastructure study.

I am here today to testify on behalf of NLC and the 16,000 cities and towns across the nation we represent on an issue of great significance to our nation's economic well-being and growth -- the ability of local governments to finance and maintain the nation's infrastructure.

Public infrastructure deterioration has become more than a threat to the health and safety of our citizens. It has also begun to affect our economy. While devastations, such as the April bridge collapse in Covington, Tennessee, highlight the urgent need for immediate attention to our infrastructure to insure the safety of our citizens, a recent report by the Federal Reserve Bank of Chicago concludes that

> a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, ports, airports, and other facilities which aid in the production and distribution of goods and services.

We believe that our willingness to invest productively in the nation's public infrastructure - to invest in our future - is critical to our ability to compete in an international economy. We now know, beyond any reasonable doubt, that the resources exist.

Shortly, we expect the President to sign legislation obligating the nation's taxpayers to spend over $200 billion dollars to bail out the nation's savings and loan industry. That is payment for past fraud, abuse, and failure, not an investment in the future.

We are here today to address what should be a more important priority. We would certainly welcome the introduction of legislation to create an ITC, Infrastructure Trust Corporation, authorizing the issuance of $50 billion in off-budget bonds to rebuild the nation. That would be a far more effective step towards confronting our trade deficit then imposing trade sanctions.

We believe there are seven guidelines the federal government should undertake to help cities and states rebuild the nation's infrastructure:

1. no further federal interference with tax exempt municipal bonds;
2. elimination of the use of effective and retroactive dates for tax exempt municipal bonds;
3. creation of a mechanism to coordinate among federal departments and agencies and within Congress to examine

and understand the implications of amendments to existing law;

4. consistency in honoring legislated commitments;
5. recognition of the impact of mandates on local priorities;
6. recognition of the fiscal capacity (or lack thereof) of local governments to comply with unfunded federal mandates and meet public infrastructure needs; and a
7. study on economic competitiveness.

Let me add, that we at the local level -- perhaps even more than you -- are very aware of the federal deficit and its impact on decisions made here in the nation's capitol. We, at the local level, perhaps more than any one else, have felt the effects of the federal government's attempts to reduce spending and get the deficit under control. Our proposals reflect our awareness of the difficult deficit problem with which you in Congress are trying to grapple.

1. No further interference with tax exempt municipal bonds:

The dramatic decline in federal financial assistance to state and local governments has resulted in severe constraints on the ability of local governments to meet the basic infrastructure needs of our communities. Local governments have increased their own revenues by raising local taxes and initiating or increasing user fees. These resources alone cannot meet the nation's infrastructure needs. Furthermore, there are limits set by state law, state constitutions, citizen initiatives and -- in this context -- most importantly, federal tax code revisions which restrict local governments' ability to raise revenues.

Capital investments at the state and local level have been and are funded largely through the use of municipal bonds.

Over the past eight years, however, the tax code has been revised no less than six times. And every time the tax code is "reformed," the ability of state and local governments to meet the infrastructure needs of our nation has been further curtailed.

In 1984, the Federal government effectively ended the concept of public-private partnerships. In 1986, the federal government effectively eliminated tax-exempt bonds. It left slightly taxable, more taxable, and fully taxable bonds.

Each and every encroachment has simply increased the cost of building, maintaining, and rebuilding housing, streets, airports, water, waste, and other public capital facilities. The so-called reforms have not limited state and municipal authority to issue capital financing, but have severely eroded the potential market for selling our bonds.

We now have volume caps, limits on the extent to which public facilities can be financed with tax exempt financing if "private purposes" are beneficiaries in excess of specified percentages; and, odd definitions of "private purposes" (Syracuse, Utah, for instance, is prohibited from using tax exempt financing for expansion of its EPA-mandated municipal wastewater plant because 17% of the treatment plant's capacity is for -- a U.S. Air Force Base -- a private purpose).

This week we anticipate the Treasury will issue arbitrage and rebate regulations, effective retroactive to September 1, 1986. These regulations will impose major new compliance costs on states and local governments and impose an effective federal tax. Instead of using this capital financing for national public infrastructure, we will take a portion for bookkeeping and rebates.

2. Use of effective and retroactive dates for tax exempt municipal bonds:

The construction of an airport, a bridge, a tertiary wastewater treatment facility is a sophisticated fiscal and engineering achievement. These are long-term projects.

Disruption imposed by unanticipated federal actions adds significant constraints and costs. One of the most severe impacts to major infrastructure projects is created by the growing practice of individual members of Congress proposing effective or retroactive effective dates in bills restricting municipal authority to use tax-exempt capital financing.

This practice is particularly unfair because it enables a single member of Congress to disrupt public financings in all parts of the nation without any report to the Congress, any hearing, any views of the administration, much less any confirmation by a majority of the Congress.

The imposition of an effective date imposes a cloud over the ability of a city, town, or state to issue a bond; for bond counsel must opine that the bond could become fully taxable to the holder, thereby reducing any incentive for its purchase.

Last year, a member of the House Ways and Means Committee proposed an amendment to the tax bill to restrict bond pool financings effective July 15, 1988. The bill had the effect of law. It precluded the Ohio Water Development Authority from issuing bonds in late July for financing water supply and wastewater construction projects in cities and towns throughout Ohio. By August we were aware of at least one infrastructure revolving loan program in 26 states adversely impacted by the amendment -- an amendment which never became law.

In August 1988, Rep. Brian Donnelly proposed legislation, to take effect this January 1, making taxable any municipal bond which failed to meet an arbitrary issuance cost cap. Only after intervention by Chairman Rostenkowski was the date rescinded. The impact would have shut down virtually any small city in America.

On March 9th, Rep. Donnelly proposed a bill to prohibit municipalities and states from issuing tax exempt bonds for the construction of publicly owned waste or wastewater facilities unless the public agency headquarters were located or relocated to the site of the waste facility. He proposed that the bill be effective March 9th for newer state and local agencies, and December 31, 1990, for all other state and local governments. That date, as far away as it may seem, is already a serious financing obstacle for any major construction planned after that date.

Earlier this month, Rep. Pete Stark proposed a bill to eliminate private activity bonds - or tax exempt bonds for housing, solid waste facilities, and other infrastructure needs, effective December 31st for any state not making certain Medicare contributions. This bill has already imposed a cloud over infrastructure financing without even any direct relationship to the Congressmen's purported concern.

I want to emphasize, Mr. Chairman and members of the committee, that we recognize and are willing to spend our day in court fighting for what we believe is appropriate public policy. We believe, however, that a practice which permits any individual in the Congress to hold public policy hostage outside of a democratic process is unfair and damaging not just to infrastructure, but to public policy.

STATEMENT OF THE
NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS

SUBMITTED FOR THE RECORD AT HEARINGS ON

INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

BEFORE THE

SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM AND THE DISTRICT OF COLUMBIA

COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
May 4, 1989

The National Association of Towns and Townships (NATaT) is pleased to submit this statement concerning intergovernmental solutions which must be brought to bear on rebuilding the nation's infrastructure. NATaT represents more than 13,000 units of general purpose local governments across the United States. These mostly small, mostly rural communities are typical of the majority of the nation's 39,000 general purpose governments, Mr. Chairman. In approaching the infrastructure issue we must remember that we are a nation of small communities Only fourteen percent of the general purpose governments in the United States below the state level serve populations over 10,000, while 72 percent of such governments serve populations of less than 3,000, and fully half of all such governments serve communities with less than 1,000 people.

These localities are significantly different than their urban and suburban counterparts in terms of staff and other resources; most have no paid staff accountants or lawyers, no professional city managers. There are no environmental engineers on the payroll, no grantspersons to secure intergovernmental aid, no major companies to invest in large public/private enterprises. These communities are the overwhelming majority of the localities in the federal-state-local partnership. They succeed on the sheer will of their dedicated public servants -- their locally elected leaders who for the most part volunteer their time and expertise as a service to their friends and neighbors in the community.

The Importance of Infrastructure in Small Communities

Mr. Chairman, small governments such as those we represent have major responsibilities in the three primary infrastructure areas which you are reviewing today: transportation, water, and solid waste disposal. Since most of the governments in the United States are small, it should come as no surprise that the task of meeting infrastructure needs rests in large part with very small communities -- those with the least ability to finance the building and maintenance of roads, bridges, water and sewer systems, and solid waste disposal facilities.

Small governments have the responsibility for the vast majority of road mileage, and tens of thousands of bridges across the United States. They have major responsibilities for providing and/or monitoring drinking water; addressing the problem of wastewater, and for meeting the stringent standards set by environmental regulations -- which for the most part have been written without regard to the resources available in small and very small governments.

And of course, the small local governments -- ten of thousands of them -- are responsible for solid waste disposal, through joint agreements with other jurisdictions, as contractors with private firms, or as principals who site and maintain solid waste disposal facilities with all the attendant problems.

The Problems

Roads and Bridges

As reported by the National Council on Public Works Improvement, the nation's infrastructure is deteriorating at an alarming rate. Over 60 percent of the nation's paved roads and a quarter of the Interstate Highway System is in need of resurfacing, according to the Federal Highway Administration (FHWA). Forty-five percent of the nation's bridges are considered obsolete or structurally deficient, and a large number of those are in small communities; on the average, one bridge collapses every two days, Mr. Chairman -- or to think of it another way, three bridges have collapsed since Monday, and another one is about to go.

More than 80 percent of the national road system is in rural areas, and nearly 70 percent is the responsibility of local governmental units; but only 20 percent is eligible for federal highway funds. Four hundred seventy thousand bridges of 20 feet or more in length have been inventoried, not to mention thousands more which are smaller. According to a recent study by USDA's Office of Transportation, the main responsibility of local governments in this area is the off-system bridges -- those not located on a Federal-Aid highway. "In 1986," the study reports, "a total of 279,091 bridges (59.4 percent) were not on the Federal-Aid system and, thus had to be financed from State and local funds." There are 9,946 such bridges in your own State of Tennessee, Mr. Chairman; 4,079 in Michigan; 1,272 in Maine; 10,204 in Pennsylvania; and 15,915 in Ohio, for example -- and those are only the inventoried bridges at least 20 feet in length.

Posted bridges in rural areas pose an enormous problem, not only for local communities but for the nation as a whole. In Pennsylvania, for example, local steel companies spend over $1 million a year detouring around the bridges which cannot support the weight of their trucks, according to the

Pennsylvania DOT. By projecting that $1 million for one industry in one state to thousands of industries in 50 states, the enormity of the economic implications becomes apparent.

Local roads also play an important role in the national economy. Some of them are farm-to-market roads; but beyond that traditional function, the role of the local road system has been significantly altered. A decreased railroad network along with changing demographics of truck transportation -- larger loads, heavier trucks -- has increased the importance of many local rural roads. According to the Federal Highway Administration, most truck vehicle miles of traffic (VMT) occur on rural roads off of the Interstate system -- and that majority will triple by the year 2020. In 1985, trucks with six or more tires logged over 30 million VMT off the Interstate system on urban roads, and 47 million VMT on rural roads off the Interstates. FHWA projects that in 2020, urban truck mileage -- again, off the Interstate -- will increase by 30 million VMT, while rural mileage will increase nearly three times that -- by nearly 90 million, to a total of 137,131 million VMT. (See chart attached). These statistics underscore the fact that the growing importance of local and rural roads to the national economy as a whole cannot be ignored.

Water and Solid Waste

The other two categories under discussion today -- water and solid waste -- are regulated by the Environmental Protection Agency (EPA), which itself admits that environmental requirements weigh most heavily against the smallest communities. Small governments, especially those below 3,000 in population (again, nearly three-fourths of all U.S. general purpose governments), find many barriers to financing, building and maintaining facilities at the level mandated by Congress and EPA. In many cases, such barriers are impossible to overcome -- leaving local officials with enormous liabilities and their citizens unprotected. Solid waste disposal looms large on the horizon for small governments. Issues such as municipal landfills and disposal of ash and sludge, will require innovative approaches on the part of federal regulators if they are to be realistically addressed. Not only is it a question of costs of maintaining appropriate facilities in many small communities, but also of whether such facilities can be built at all, given that part-time local officials may not have the level of expertise which will enable them to negotiate successfully with state and federal agencies, lenders, or compete for loans, grants, or other financing.

Small Communities -- Failures, or Keys to the Future?

Without adequate infrastructure, small communities cannot compete. The state of our infrastructure is a serious problem for our nation as a whole; for small communities, it is a matter of survival. Infrastructure is our tie to the outside world; the sledge hammer which breaks down walls of isolation and allows the world to connect. It can also play a key role in creating economic opportunity -- not only for small communities, but for all of America's citizens.

There are major changes at work across this country. Entrepreneurs, service industries, and corporate entities are reaching out to take advantage of emerging technology which enables them to do business anywhere; to move out of large metropolitan areas to towns and villages where the cost of living is lower and the quality of life is higher. The public is ahead of the curve on this one, Mr. Chairman; already investment bankers operate from small towns rather than from New York City; publishing houses, insurance companies, and accounting firms, have moved to small communities; free-lance consultants, data processors, and other service providers are moving back out to the country. And it is happening almost faster than we can recognize.

A Mixed Blessing

The potential of this rural renaissance can be viewed as a mixed blessing. On one hand, it would alleviate congestion and subsequent pressure for our urban centers by creating new opportunities in rural America. On the other hand, rural infrastructure problems will grow greater with new demands, reaching beyond the traditional categories under discussion today. We need to address telecommunications technology; the tremendous demand for fiber optics and effective two-way interchanges not only in high density areas, but throughout the United States. And it means that the needs of our rural health care system -- hospitals, clinics, and emergency medical services -- demand an even higher level of priority.

Financing in Local Government

Mr. Chairman, small governments cannot absorb infrastructure costs alone. In many cases, small community resources are not adequate to meet current needs, much less to develop additional capacity. For the most part, small governments can only rely on the property tax as their chief financing means. As you know, property values in many small communities are declining. Financing mechanisms which are commonplace in larger communities are not always available to small governments, and economies of scale work against them. It is not unusual for small governments to hold raffles and bake sales to supplement annual budgets; such fundraising activities take place in thousands and thousands of governments nationwide.

Although user fees have played an important role in maintaining some forms of infrastructure, particularly in the areas of water, wastewater and solid waste, small governments generally are only able to make limited use of this financing technique. Spreading costs on a per capita basis, as user fees do, is not realistic in very small places where the population is too low to keep costs reasonable. Consequently, small communities can only raise a portion of the costs through user fees; the remainder must be subsidized either by intergovernmental transfers or by bond financing.

Intergovernmental Transfers

In recent years, intergovernmental transfers have been only minimally effective in providing support to small town America because they have been so drastically reduced, and because most programs are not designed to take into account the unique circumstances of small governments. Those federal programs which have helped to finance small town and rural America's infrastructure include the Farmer's Home Administration water and wastewater loans and grants, community facilities loans and grants, EPA's wastewater construction grants programs, the Federal Aid Highway System -- primarily the Secondary (Rural) Highway System and Off-Systems bridge program, Appalachian Highway System, and the Community Development Block Grant Small Cities Program.

Over all, programs that were providing funding for rural America have been cut by over 67 percent since 1980. The Secondary Highway System has lost over 60 percent of its funding in the past decade; in this same period FmHA's water and waste disposal grants program lost nearly 75 percent, water and waste disposal loans lost nearly 65 percent, and the community facilities loans have gone down nearly 80 percent. EPA's construction grants program has been cut by over three-fourths in the last ten years; and the Community Development Block Grant Small Cities program lost one-third of its funding in this same period. Since the elimination of the General Revenue Sharing (GRS) program, 80 percent of the general purpose local governments in the United States receive absolutely no federal funding.

THE INTERGOVERNMENTAL ISSUE

Do these reductions mean that the demand on infrastructure has been reduced? No. Do they signal a decrease in federal mandates, allowing local governments to alter requirements and shift priorities? No. Do they mean that local governments are doing better financially, and thus are more able to shift their own resources to fill the void. Obviously not. What these reductions do mean is that the federal/local partnership has been broken -- that the federal partner has not lived up to its responsibility for marshalling national resources to address national issues. Our infrastructure is a national priority.

Not only has the federal government withdrawn its support, it has exacerbated the problems at the local level by building barriers. This is nowhere more evident than in the case of tax-exempt bond financing. Bond issuance is perhaps the most important financing tool presently at the disposal of local governments. Obviously, infrastructure costs -- new construction and expansion in particular-- are big ticket items. Water systems, wastewater systems, solid waste facilities, new bridges and roads -- cannot be funded on the property tax alone. They cannot be funded by user fees. They cannot be funded by bake sales. The federal government has already eliminated the General Revenue Sharing program which for many years was used by small governments to finance major facilities; and, as we have already discussed, most federal aid to small and local government has fallen victim to the budget cutting ax.

Tax-Exempt Financing: the Next Budget Target

In many cases, the only tool left to small and local government is tax-exempt financing. Although this mechanism is not directly available to thousands of very small communities, those which are somewhat larger have been able to use tax-exempt financing to fund their first wastewater systems, to expand these systems to meet new growth demands, and to replace aging systems, which no longer meet federal standards. Such financing is crucial to raising the millions of dollars required for building safe drinking water systems for small and growing communities. And it will become increasing more important as communities -- small and large alike -- begin to face increasingly urgent environmental issues, including new rules and regulations in the areas of solid waste disposal and ground water protection.

Even though it may be the only remaining mechanism for many local governments, tax-exempt financing is under attack. In its rush to find new revenue sources, Congress is considering eliminating this vital tool. Without tax-exempt financing, governments -- small and large alike -- cannot hope to make even a small dent in the nation's infrastructure needs. Water systems, waste facilities, and sewer systems simply will not be built. Bridges will continue to collapse and roads will continue to deteriorate; storm systems simply will not exist; our communities and our neighbors will be placed at even greater risk.

Pay Now or Pay Later

Mr. Chairman, simply put, we can pay now or pay later. Working through a true cooperative partnership which includes the federal, state, and local governments, we can design programs to begin to address our infrastructure needs. Or we can wait until it is a full-blown crisis -- until our communities collapse around us -- and costs to replace and repair will soar beyond our wildest imagination.

There is no way of getting around the costs, and costs will never be lower. The American public trusts their local, state and federal elected leaders to provide leadership, but the federal government is letting them down -- it is playing with smoke and mirrors -- while knowing that it is placing the future of the nation at risk.

RECOMMENDATIONS

There are no easy solutions for this national problem; but there are a number of recommendations that our association suggests to you today.

First and foremost, we urge Congress and the Administration to recognize that rebuilding the nation's infrastructure is a national priority. This critical issue must be considered as such in setting national priorities -- budgetary and non-budgetary policies -- developed by Congress and the Administration. Most importantly, the federal government must assume its share of the responsibility for rebuilding our nation's infrastructure.

In recognizing its responsibility, the federal government must once again acknowledge local governments as partners in providing essential services to America's citizens, and must stop targeting local government -- particularly small local government -- for revenues.

This means that the federal government must work to strengthen and preserve the fiscal capacity of local governments to address the nation's infrastructure problems in all future federal policies. Tax exempt financing must be preserved. Discretionary programs that finance infrastructure must received a new priority. And the Highway Trust Fund must be used for its original purposes -- to repair and maintain our national system of roads and bridges. All trust fund monies must be allocated for their intended purpose, and not held hostage to meet Gramm/Rudman/Hollings targets. In addition, the gasoline tax, which funds our national road network, must continue to be dedicated for highway expenditures; it must not be invaded for deficit reduction purposes. All efforts should be made to fund these programs proportionately to meet this emerging priority.

From a small local government perspective, federal policymakers must rethink federal assistance programs to ensure that funds are targeted for small communities. Federal programs which allocate funds on a per capita basis will never address the critical problems facing many of the nation's smaller communities, because they inherently direct funds away from these communities in favor the nation's larger cities. Formulas that allocate funds on a per capita basis do not belong in any national program that realistically attempts to address a national problem. If a true federal/local partnership is to exist, the federal government must recognize the bias against small communities which has become inherent in our federal assistance system: per capita and tax effort measurements are perfect examples.

Such criteria essentially prevents funding from reaching small communities. Since most small governments have no staff or professional expertise at their disposal, they cannot compete in an assistance system which requires sophisticated grantsmanship skills in order to succeed. Federal criteria should be based on need. Federal agencies should be required to establish outreach mechanisms to provide assistance in the form of planning, technical assistance, and grantsmanship in order to offer small communities the same access to federal assistance which is currently made available to their larger counterparts.

Rethinking national criteria for federal assistance must be done before the Federal Aid Highway program is reauthorized. With the completion of the interstate system by 1991, a greater share of the trust funds must be directed toward local roads and bridges where there is the greatest need. This includes not only country roads, but also roads within our towns, townships, and small communities. Small town America must be brought into the process as we rethink our federal aid highway system; small communities must receive their fair share of these funds, and state government must be required to work with these small communities in any state planning or priority setting for use of these monies.

Finally, Congress and the Administration must recognize that they must begin to assess priorities as they mandate local governments to implement federal policies. We cannot afford to pay for federally regulated requirements in the areas of clean water, safe drinking water, underground storage tanks, storm sewers, flood plain, clean air, hazardous waste, emergency response, and on and on. It is not that we disagree with these objectives, but rather we simply do not have the resources to pay for requirements which are all to often based on unrealistic expectations and a misunderstanding of local capacities. There is absolutely no federal accounting of the total costs to local government for federally mandated national priorities. Mr. Chairman, it is so easy to mandate local governments to do certain things, but impossible at best to ensure that local governments can indeed meet these requirements.

It is for this reason that NATaT began its campaign several years ago to solicit support for a new rationale regulatory process which takes into account the ability of a small local government to meet national mandates and to work these small communities to devise regulations that make sense. As you know, Mr. Chairman, we believe that the Regulatory Flexibility Act of 1980, amended as we have recommended to the full committee, will begin this rationale federal policy process

Our recommendations for improving the Reg Flex Act would remove the loophole which allows agencies to ignore the Law and would ensure that agencies consider alternatives in establishing national guidelines -- adjusting requirements to local capacities.

In addition, we have also recommended that the General Accounting Office be required to assess current federal efforts to collect data on small governments, to establish national standards for data gathering which allow for the sharing of information and encourages the sharing of data from agency to agency. We also believe that Congress should require reports from federal agencies which assess the cumulative burden of mandates on small governments. These recommendations have been forwarded to the full committee chairman, Senator Glenn. We urge this subcommittee to support our efforts to secure passage of new legislation in this regard.

In addition, we also believe that Congress itself could do a better job at policing new mandates on local governments through using cumulative data when considering new policies and establishing priorities. A process which takes a hard and realistic look at specific proposed policies in the formulation stage -- that is as bills are drafted -- and considers these proposed policies within the context of what small local governments are already expected to do, makes a great deal more sense than the current process.

KEEPING THE DOOR OPEN

In Conclusion, Mr. Chairman, there is a lot more at stake here than the traditional dream of "small town America." By ignoring small communities, the federal government is closing a bright door to our nation's future. If small communities are forced to fail -- if they fade away, and their children continue to migrate to larger communities looking for homes and jobs -- big city infrastructure problems will grow exponentially. If you think New York City has problems now, or Chicago, or Los Angeles -- or Washington, D.C. -- imagine what it would be like if they were the only alternative! It is clearly in the interest of large and small communities alike to preserve the choices, to encourage economic development in rural areas, and to reduce the pressure on the urban infrastructure. Viewing the problem in its entirety -- from the perspective of urban centers, small communities, and the places in between -- our national interest lies in a secure intergovernmental partnership, forming a solid foundation for current and future infrastructure investment.

Mr. Chairman, on behalf of tens of thousands of small governments across this nation, thank you for your concern and your support. We applaud you and the committee members for recognizing the importance of this issue and for scheduling this hearing today. NATaT appreciates the opportunity to present this statement, and we would be happy to respond to any questions.

Thank you.

STATEMENT FOR THE RECORD
BY ROBERT B. HAWKINS, JR., CHAIRMAN
U.S. ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS

HEARING ON INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM, AND THE DISTRICT OF
COLUMBIA, COMMITTEE ON GOVERNMENTAL AFFAIRS

MAY 4, 1989
WASHINGTON, DC

I am pleased to present testimony for the Advisory Commission on Intergovernmental Relations (ACIR) on America's infrastructure problems and intergovernmental solutions. Infrastructure has been an intergovernmental responsibility since the beginning of our federal republic, and the ACIR itself has a long record of involvement in infrastructure matters. Most recently, moreover, the ACIR provided supportive administrative services to the National Council on Public Works Improvement (NCPWI) during its life, and then assumed responsibility for archiving its records and disseminating its reports after NCPWI was terminated in 1988. The ACIR also has had discussions with the American Public Works Association regarding its proposals to the Congress that the ACIR be made the focal point in the federal government for public works, precisely because the ACIR is an independent, bipartisan, intergovernmental agency. There is no focal point now.

Salient issues that frame any discussion of infrastructure today include the following: (1) the nation's infrastructure is, as NCPWI phrased it, fragile, but not in ruins; (2) substantial investment is needed to upgrade the nation's infrastructure, but public revenue is in short supply; (3) more revenue is not the only solution, or always the best solution; and (4) infrastructure improvements are needed not only to improve the nation's competitive position worldwide but also to improve the quality of life, enhance economic opportunities for all Americans, and provide a solid foundation for our children's prosperity.

Five crucial questions need to be addressed with respect to infrastructure upgrading. (1) Rather than assuming that government must always increase supply in response to demand, how can we reduce inefficient and non-economically viable demands on the nation's infrastructure (e.g., inefficient uses of water)? (2) How can we link costs more closely to benefits without sacrificing equity? (3) What is the appropriate mix of public and private sector provision and production of infrastructure? (4) How can we improve the capabilities of local governments, primarily, as well as state governments, to maintain and upgrade public and private sector infrastructure investments? (5) How can we improve the compatibility of the policies and services provided by different governments, especially those of larger jurisdictions that serve smaller jurisdictions? The answers to all five questions involve intergovernmental cooperation so that federal, state, and local governments do not work at cross purposes.

Intergovernmental coordination needs to be improved in three areas: (1) fiscal policy, (2) regulatory policy, and (3) communications and planning. Coordination has taken on heightened importance because of two recent trends: (1) state and local governments have been assuming more public-works responsibilities and (2) the privatization of public works has been increasing.

Fiscal Policy

Federal aid to state and local governments for public works has declined in recent years while state and local own-source spending has increased. Overall public-works spending has risen, but new capital investment--the traditional emphasis of federal aid--has slipped, as have major maintenance and rebuilding of existing structures. Given that states have only partly replaced lost federal-aid revenues, local governments are bearing a greater infrastructure burden.

Several issues need to be addressed in any reform of federal fiscal policies. For one, federal aid sometimes stimulates unnecessary demand for infrastructure services and sometimes constrains state and local governments to provide services that are less than optimal or efficient. At the same time, there is insufficient aid for basic research, development, and demonstration projects.

Federal tax incentives for private public-works investment have been reduced dramatically, thus making it more difficult for state and local governments to create public-private partnerships. In addition, state and local infrastructure financing is being based increasingly on user fees, which are not deductible from federal income-tax liabilities. Indeed, sales taxes also are no longer deductible; yet, they are an important source of dedicated funds for local transit systems. A related issue is the non-deductibility of the fees paid to the growing number of residential community associations that maintain streets and other infrastructure services normally provided by local governments. (Shortly, the ACIR will issue a report on these "private governments.") Furthermore, given that tax-exempt bonds are very important in infrastructure financing, the 1986 limits on such bonds should be watched closely and loosened if they prove to be too restrictive.

With respect to state and local fiscal capacities, scarce federal dollars can be better targeted to areas of greatest need and of least own-source fiscal capacity. The ACIR's measures of state fiscal capacity and its current work on measures of state spending needs provide tools for improving federal-aid targeting.

Regulatory Policy

A variety of regulatory issues need to be addressed, beginning with the largely unsystematic and de facto devolutions of federal responsibilities that have been occurring since the late 1970s. In addition, federal funds that are available for public works are often subject to considerable uncertainties that make it difficult for state and local governments to plan and spend effectively. In some cases, such as highways, moreover, so-called demonstration programs are little more than pork-barrel projects. For these and other reasons, the ACIR has endorsed the devolution of selected federal-aid programs and revenue bases, and has suggested ways to do so.

Unfunded federal mandates and regulatory complexity also make it difficult for states and localities to manage infrastructure problems. The "fiscal notes" process in the Congress and Executive Order 12612 do not appear adequate in their present forms to resolve the problems arising from unilateral federal actions.

Attention must be given as well to legislative and bureaucratic fragmentation within state governments and the federal government. More and more, local governments have been able to overcome jurisdictional fragmentation in order to resolve infrastructure problems, only to confront fragmentation and delays in the state and federal arenas. In other words, state and federal "rules of the game" are no less important, and sometimes more important, than state and federal aid in helping or allowing local governments to solve problems.

Similarly, the federal government must be attentive to regulations that may quash state and local efforts to reduce infrastructure demands. For example, Minneapolis recently passed an ordinance banning nonrecyclable plastic at food stores and restaurants so as to reduce demand on the city's solid-waste disposal facilities and enhance environmental protection. Industry representatives plan to challenge the ordinance in federal court as an unconstitutional restraint on interstate commerce. The ACIR has taken no position on this or similar ordinances, but the case does illustrate a looming problem, namely, overinterpretation of federal powers under the commerce clause, which may increasingly frustrate state and local efforts to resolve the demand side of infrastructure problems. This obstacle is likely to extend to innovative pricing mechanisms as well.

Communications and Planning

The changing federal role in public works, uncertainty in federal funding, regulatory complexity, legislative and bureaucratic fragmentation, and federal court interventions have all made it difficult for governments in the federal system to communicate and plan effectively for infrastructure development. Hence, the federal government must carve out for itself a role that is reasonably stable, predictable, and supportive of state and local initiatives. Given the fiscal constraints facing all governments in the federal system as well as the novel infrastructure problems we face today, it makes sense to encourage diversity and experimentation. Furthermore, given the expertise increasingly available to states and localities, a facilitative role and, where necessary, compensatory role, seems appropriate for the federal government.

Although, for this hearing, I have focused my comments on problems and issues in the federal government's infrastructure role, state and local governments also need to address problems in their own policies and practices.

I thank you for the opportunity to present this testimony. I have only scratched the surface of infrastructure issues in the federal system; however, the ACIR remains prepared to provide continuing assistance to the Congress on these important issues.

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State Highway Funding Sources

State	Fed. Aid	M/F Taxes	Veh. Regis.	Misc. Truck Fees	Drivers Lic.	Bonds	Gen. Fund	Misc.
AL	47.4%	25.8%	8.0%	—%	—%	8.7%	—%	7.4%
AK	60.0	—	—	—	—	—	40.0	—
AZ	23.1	34.6	8.7	10.8	0.7	6.9	1.4	13.8
AR	28.9	46.9	14.3	4.1	1.2	—	—	4.6
CA	46.0	23.0	—	—	—	—	—	31.0
CO	35.7	49.1	5.2	5.1	0.8	—	—	4.1
CT	37.8	22.2	9.4	—	1.4	22.8	—	6.4
DE	35.5	21.7	—	2.4	—	—	40.4	—
DC	38.0	16.0	8.0	—	1.0	23.0	14.0	—
FL	38.0	—	18.0	—	—	—	—	44.0
GA	28.6	29.7	—	—	—	16.3	1.5	23.9
HI	38.0	33.1	5.7	0.4	—	—	—	22.8
ID	40.6	33.8	13.0	8.4	0.8	—	—	3.4
IL	24.6	34.4	27.0	—	1.6	4.0	4.3	4.1
IN	28.0	53.0	13.0*	—	—	—	4.0	2.0
IA	26.1	33.7	24.7	—	1.2	—	—	14.3
KS	41.0	27.0	19.8	1.0	1.0	—	5.6	4.6
KY	21.5	32.5	5.0	0.3	0.5	14.9	—	25.3
LA	31.0	20.0	—	—	—	43.0	6.0	0.0
ME	25.6	37.0	16.2	—	1.4	4.8	5.0	10.0
MD	25.0	27.0	8.0	1.0	—	—	—	39.0
MA	12.7	51.8	26.9*	—	—	—	0.1	8.5
MI	23.0	45.5	24.5	1.0	0.5	—	—	5.5
MN	30.8	33.4	20.7	—	1.3	—	—	13.8
MS	47.0	35.0	—	—	—	—	—	18.0
MO	27.5	36.6	20.3	0.4	1.2	—	—	14.0
MT	40.6	41.0	—	9.8	—	—	—	8.6
NE	29.7	42.0	12.0	—	—	—	—	16.3
NV	28.0	34.0	9.1	10.2	1.2	14.8	—	2.7
NH	33.0	41.7	22.3*	—	—	—	—	3.0
NJ	44.4	10.8	—	—	—	9.6	35.2	—
NM	30.2	34.9	9.0	11.5	1.0	—	—	13.4
NY	30.0	—	—	—	—	10.0	60.0	—
NC	23.2	52.5	16.6	—	3.2	—	—	4.5
ND	44.0	34.8	15.1	1.7	1.3	—	—	3.1
OH++	46.5	32.7	0.1	—	—	—	—	20.7
OK	45.9	48.8	0.2	—	—	—	2.3	2.8
OR	20.0	27.0	10.0	20.0	2.0	12.0	—	9.0
PA	30.6	25.4	12.3	0.6	1.8	2.6	—	26.7
RI	51.0	—	—	—	—	13.0	36.0	—
SC	32.2	52.2	9.2	0.1	1.1	—	0.2	5.0
SD	44.6	36.4	2.2	—	—	—	—	16.8
TN	35.6	37.6	16.2	—	—	7.0	—	3.6
TX	31.7	37.9	21.7	—	—	—	—	8.7
UT	41.5	46.6	6.4	2.3	1.6	—	0.3	1.3
VT	35.2	25.0	18.9	—	—	—	—	20.9
VA	19.9	35.1	5.8	2.0	—	—	—	37.2
WA	35.1	42.8	15.8	—	—	3.2	—	3.1
WV	41.3	30.4	9.4	—	0.5	—	—	18.4
WI	21.5	46.9	17.0	—	1.5	4.2	—	8.9
WY	36.4	12.4	14.7	—	—	—	2.1	34.4

*— Includes vehicle registrations and drivers' licenses
++ – 1987 data (1988 data unavailable)

SOURCE: TRIP-THE ROAD INFORMATION PROGRAM

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PROSPECTUS
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PROSPECTUS

January 27, 1989

Tax Exempt Proceeds Fund, Inc. (the "Fund") is a diversified, short-term, tax exempt money market fund that seeks to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and maintenance of liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" for Federal income tax purposes and, therefore, shareholders of the Fund that are tax exempt bond issuers, in the opinion of counsel, are expected to be exempt from the arbitrage rebate provisions of the Internal Revenue Code of 1986, as amended (the "Code"). The Fund seeks to achieve its objectives by investing primarily in a liquid money market portfolio of short-term, high quality, tax exempt fixed rate and variable rate obligations issued by state and municipal governments and by public authorities, and in participation interests therein issued by banks, insurance companies or other financial institutions that meet this Federal income tax definition. There can be no assurance that the Fund's objectives will be achieved.

The shares of the Fund will be offered primarily to entities that are issuers of tax exempt state and local bonds, such as states and municipalities and their authorities, agencies, instrumentalities and subdivisions ("Qualified Investors".)

This Prospectus sets forth concisely the information about the Fund that prospective investors will find helpful in making their investment decisions. This Prospectus should be read and retained by investors for future reference. A Statement of Additional Information dated the same date as this Prospectus containing additional information about the Fund has been filed with the Securities and Exchange Commission and is incorporated by reference into this Prospectus in its entirety. Additional copies of this Prospectus and copies of the Statement of Additional Information may be obtained on request and without charge from the Fund directly.

Reich & Tang L.P. acts as manager of the Fund and distributor of the Fund's shares. Reich & Tang L.P. is a registered investment adviser and a registered broker-dealer and member of the National Association of Securities Dealers, Inc.

The Fund intends to maintain a constant net asset value of $1.00 per share although there can be no assurance that this value will be maintained.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

INTRODUCTION

Tax Exempt Proceeds Fund, Inc. (the "Fund") is a diversified, open-end management investment company that seeks to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" for Federal income tax purposes and, therefore, Fund shareholders that are tax exempt bond issuers are expected to be exempt from the arbitrage rebate provisions of the Code. (See "Investment Objectives and Policies ".) The Fund seeks to achieve its objectives by investing principally (and in no event less than 98% of its assets) in short-term, high quality fixed rate and variable rate tax exempt securities issued by state or municipal governments and by public authorities that meet this Federal income tax definition and in participation certificates therein purchased from banks and other financial institutions. However, the Fund will not concentrate its investments in participation certificates. The Fund's portfolio will be invested primarily in municipal obligations, including municipal notes and industrial revenue bonds (issued before August 8, 1986). The Fund's investments may also include when-issued securities. The Fund will not invest in securities the interest income on which may be subject to the individual alternative minimum tax. The Fund seeks to maintain an investment portfolio with a dollar-weighted average maturity of 120 days or less, and to value its investment portfolio at amortized cost and maintain a net asset value of $1.00 per share. This is a summary of the Fund's fundamental investment policies which are set forth in full under "Investment Objectives and Policies" in this Prospectus and in the Statement of Additional Information and may not be changed without the approval of a majority of the Fund's outstanding shares; except that the Fund's fundamental investment policies of investing in securities that would qualify an investment in the Fund as a "tax exempt bond" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax may only be changed with the approval of 90% of the Fund's outstanding shares.

There can be no assurance that the Fund's objectives will be achieved. Investment by the Fund in other than "tax exempt bonds" will subject the Fund's shareholders that are tax exempt bond issuers to the arbitrage rebate provisions of the Code. However, the Fund's fundamental investment policies prohibit the Fund from investing in other than "tax exempt bonds".

The Fund's investment manager is Reich & Tang L.P. (See "Management of the Fund".) The Fund's shares are distributed through Reich & Tang L.P., with whom the Fund has entered into a Distribution Agreement pursuant to the Fund's plan adopted under Rule 12b-1 under the Investment Company Act of 1940, as amended (the "Act"). (See "Distribution Plan".)

The shares of the Fund will be offered primarily to entities that are issuers of tax exempt state and local bonds, such as states and municipalities and their authorities, agencies, instrumentalities and subdivisions ("Qualified Investors").

The Fund's investment policies were developed for the particular Federal income tax needs of Qualified Investors. Investors that are not issuers of state and local bonds and that desire to invest in a tax exempt money market fund may consider an investment in the other tax exempt money market funds managed by Reich & Tang L.P.

On any day on which the New York Stock Exchange, Inc. is open for trading ("Fund Business Day"), investors may, without charge by the Fund, initiate purchases and redemptions of shares of the Fund's common stock at their net asset value, which will be determined daily. (See "How to Purchase and Redeem Shares" page 7 and "Net

TABLE OF FEES AND EXPENSES

Annual Fund Operating Expenses

(as a percentage of average net assets)

Management Fees	0.40%
Other Expenses – After Reimbursement of Expenses	-0-
Total Fund Operating Expenses	0.40%

Example	**1 year**	**3 years**
You would pay the following expenses on a $1,000 investment, assuming 5% annual return (cumulative through the end of each year):	$ 4	$ 13

The purpose of the above fee table is to assist an investor in understanding the various costs and expenses that an investor in the Fund will bear directly or indirectly. For a further discussion of these fees see "Management of the Fund" and "Distribution Plan" herein. The Manager has agreed to bear or reimburse all the expenses of the Fund (other than the Management Fee); absent such reimbursement, Other Expenses would have been .26% based upon estimated expenses for the first fiscal year. However, the terms of the Management Contract provide that all such expenses must be borne by the Manager. The figures reflected in this example should not be considered as a representation of past or future expenses. Absent the Manager's obligation to bear the Fund's expenses, actual expenses may be greater or lesser than those shown above.

Asset Value", page 13.) Dividends from accumulated net income are declared by the Fund on each Fund Business Day. The Fund pays interest dividends monthly on the last day of each month or, if the last day of each month is not a Fund Business Day, on the preceding Fund Business Day. Net capital gains, if any, will be distributed annually, within 45 days after the end of the Fund's fiscal year. All dividends and distributions of capital gains are automatically invested in additional shares of the Fund unless a shareholder has elected by written notice to the Fund to receive either of such distributions in cash. (See "Dividends and Distributions", page 7.)

INVESTMENT OBJECTIVES AND POLICIES

The Fund is a diversified, open-end, investment company whose investment objectives are to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" as defined in Section 150(a)(6) of the Code and amplified by IRS Notice 87-22 and, therefore, shareholders of the Fund that are tax exempt bond issuers are expected to be exempt from the arbitrage rebate provisions of the Code. There can be, of course, no assurance that the Fund will achieve its investment objectives.

The Fund's assets will be invested principally (and in no event less than 98%) in short-term, high quality, fixed rate and variable rate tax exempt securities issued by or on behalf of states and municipal governments, and their authorities, agencies, instrumentalities and political subdivisions that meet this Federal income tax definition ("Municipal Obligations") and in participation certificates in such obligations purchased from banks, insurance companies or other financial institutions. The Fund will not invest in Municipal Obligations or any other securities the interest income on which may be subject to the individual alternative minimum tax. The Fund seeks to maintain an investment portfolio with a dollar-weighted average maturity of 120 days or less, and to value its investment portfolio at amortized cost and maintain a net asset value of $1.00 per share. The Fund may hold uninvested cash reserves pending investment. The Fund's investments may include "when-issued" Municipal Obligations and standby commitments (however, the Fund expects to invest less than 5% of its assets in such). The Fund expects to invest in participation certificates purchased from banks in industrial revenue bonds and other Municipal Obligations. The Fund will not invest in IRBs issued after August 7, 1986 the interest income from which may be subject to the individual alternative minimum tax. In view of this investment in bank participation certificates in Municipal Obligations, an investment in the Fund should be made with an understanding of the characteristics of the banking industry and the risks which such an investment may entail. See "Variable Rate Demand Instruments and Participation Certificates" in the Statement of Additional Information. The investment objectives of the Fund described in this paragraph may not be changed unless approved by a majority of the holders of the outstanding shares of the Fund that would be affected by such a change; except that the Fund's fundamental policies of investing in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax, may only be changed with the approval of 90% of the Fund's outstanding shares.

In view of the investment of the Fund in IRBs (issued before August 8, 1986) and participation interests therein secured by letters of credit or guarantees of banks, an investment in Fund shares should be made with an understanding of the characteristics of the banking industry and the risks which such an investment may entail. Banks are subject to extensive governmental regulations which may limit both the amounts and types of loans and other financial commitments which may be made and interest rates and fees which may be charged. The profitability of this industry is largely dependent upon the availability and cost of capital funds for the purpose of financing lending operations under prevailing money market conditions. Also, general economic conditions play an important part in the operations of this industry and exposure to credit losses arising from possible financial difficulties of borrowers might affect a bank's ability to meet its obligations under a letter of credit.

The Fund has adopted the following fundamental investment restrictions which may not be changed unless approved by a majority of the outstanding shares of the Fund. The Fund is subject to further investment restrictions that are set forth in the Statement of Additional Information. The Fund may not:

1. Borrow Money. This restriction shall not apply to borrowings from banks for temporary or emergency (not leveraging) purposes, including the meeting of redemption requests that might otherwise require the untimely disposition of securities, in an amount up to 15% of the value of the Fund's total assets (including the amount borrowed) valued at market less liabilities (not including the amount borrowed) at the time the borrowing was made. While borrowings exceed 5% of the value of the Fund's total assets, the Fund will not make any investments. Interest paid on borrowings will reduce net income.

2. Pledge, hypothecate, mortgage or otherwise encumber its assets, except in an amount up to 15% of the value of its total assets and only to secure borrowings for temporary or emergency purposes.

3. Purchase securities subject to restrictions on

disposition under the Securities Act of 1933 ("restricted securities"), except the Fund may purchase variable rate demand instruments which contain a demand feature. The Fund will not invest more than 10% of the Fund's total net assets in securities that are not readily marketable (including participation certificates and variable rate demand instruments with a right to demand payment on more than 7 days notice).

4. Invest more than 25% of its assets in the securities of "issuers" in any single industry, provided that the Fund may invest more than 25% of its assets in bank participation certificates. With respect to 75% of the total amortized cost value of the Fund's assets, not more than 5% of the Fund's assets may be invested in securities that are subject to underlying puts from the same institution, and no single bank shall issue its letter of credit and no single financial institution shall issue a credit enhancement covering more than 5% of the total assets of the Fund. However, if the puts are exercisable by the Fund in the event of default on payment of principal and interest on the underlying security, then the Fund may invest up to 10% of its assets in securities underlying puts issued or guaranteed by the same institution; additionally, a single bank can issue its letter of credit or a single financial institution can issue a credit enhancement covering up to 10% of the Fund's assets, where the puts offer the Fund such default protection.

5. Invest in securities of other investment companies.

The Fund's Board of Directors has determined that the term "high quality" currently means Municipal Obligations that at the time of purchase are rated at least either "AAA" or "AA" by Standard & Poor's Corporation ("Standard & Poor's") or "Aaa" or "Aa" by Moody's Investors Service, Inc. ("Moody's") in the case of bonds; "SP-1" by Standard & Poor's or "MIG-1" or "MIG-2" by Moody's in the case of notes; "A-1" or "A-2" by Standard & Poor's or "Prime-1" by Moody's in the case of tax exempt commercial paper; "SP-1/AA" by Standard & Poor's or "VMIG-1" or "VMIG-2" by Moody's in the case of variable and floating rate demand notes, or which are unrated but are determined to be of minimal credit risk and of comparable quality by the Fund's Board of Directors on the basis of its credit evaluation of the issue, which may include an evaluation of a letter of credit, guarantee, insurance or other credit facility issued in support of the Municipal Obligations or participation certificates. (See "Variable Rate Demand Instruments and Participation Certificates" in the Statement of Additional Information.) Such instruments may produce a lower yield than would be available from less highly rated instruments. If a substantial portion of the Fund's assets are invested in such unrated demand notes, the inability of the issuers to pay such notes on demand could adversely affect the Fund's liquidity.

All investments by the Fund will mature or will be deemed to mature within one year from the date of acquisition and the average maturity of the Fund's portfolio (on a dollar-weighted basis) will be 120 days or less.

For purposes of determining whether a variable rate demand instrument held by the Fund matures within one year from the date of its acquisition, the maturity of the instrument will be deemed to be the longer of (1) the period required before the Fund is entitled to receive payment of the principal amount of the instrument through demand or (2) the period remaining until the instrument's next interest rate adjustment. The maturity of a variable rate demand instrument will be determined in the same manner for purposes of computing the

Fund's dollar-weighted average portfolio maturity.

It is anticipated that Qualified Investors will utilize the Fund for short-term investment purposes. While this may result in a high rate of portfolio turnover with increased transaction costs, it will not affect the Fund's expense ratio because of the Manager's obligation to pay all expenses of the Fund (other than the management fee).

MANAGEMENT OF THE FUND

The Fund's Board of Directors, which is responsible for the overall management and supervision of the Fund, has employed Reich & Tang L.P. (the "Manager") to serve as investment manager of the Fund. The Manager provides persons satisfactory to the Fund's Board of Directors to serve as officers of the Fund. Such officers, as well as certain other employees and directors of the Fund, may be directors or officers of Reich & Tang, Inc., the sole general partner of the Manager or employees of the Manager or its affiliates. Due to the services performed by the Manager, the Fund currently has no employees and its officers are not required to devote full-time to the affairs of the Fund. The Statement of Additional Information contains general background information regarding each director and principal officer of the Fund.

The Manager is a Delaware limited partnership with its principal office at 100 Park Avenue, New York, New York 10017. The Manager was at December 31, 1988 manager, advisor or supervisor with respect to assets aggregating in excess of $8 billion. Messrs. Oscar L. Tang, Joseph H. Reich and Robert F. Hoerle, who are officers, directors and shareholders of Reich & Tang, Inc., the sole general partner of the Manager, may each be deemed a "controlling person" of the Manager. The Manager acts as manager or administrator of fourteen other investment companies and also advises pension trusts, profit-sharing trusts and endowments.

Pursuant to the Management Contract, the Manager manages the Fund's portfolio of securities and makes decisions with respect to the purchase and sale of investments, subject to the general control of the Board of Directors of the Fund.

The Manager also performs clerical, accounting and office service functions for the Fund and provides the Fund with personnel to perform accounting and related services, calculate net asset value and yield, prepare reports to and filings with regulatory authorities, and perform such other services as the Fund may from time to time request of the Manager. The personnel rendering such services may be employees of the Manager or its affiliates.

For its services under the Management Contract, the Manager receives from the Fund a fee equal to .40 of 1% per annum of the Fund's average daily net assets up to $250 million; .35 of 1% per annum of the average daily net assets between $250 million and $500 million; and .30 of 1% per annum of the average daily net assets over $500 million for managing the Fund's investment portfolio and performing related administrative and clerical services. The Management Contract also provides that the Manager will bear the cost of, or reimburse the Fund for, all other expenses of the Fund. Therefore, the fee payable under the Management Contract will be the only expense of the Fund. The fees are accrued daily and paid monthly. Any portion of the total fees received by the Manager may be used by the Manager to provide shareholder and administrative services and for distribution of Fund shares. (See "Distribution Plan", page 11.)

DESCRIPTION OF COMMON STOCK

The Fund was incorporated in Maryland on

November 18, 1988. The authorized capital stock of the Fund consists of twenty billion shares of common stock having a par value of one-tenth of one cent ($.001) per share. Each share when issued has equal dividend, distribution and liquidation rights and each unanimous share has rights in proportion to the percentage it represents of a whole share. There are no conversion or preemptive rights in connection with any shares of the Fund. All shares when issued in accordance with the terms of the offering will be fully paid and nonassessable. Shares of the Fund are redeemable at net asset value, at the option of the shareholders. On January 5, 1989 the Manager purchased 100,000 shares of the Fund at an initial subscription price of $1.00 per share.

The shares of the Fund have non-cumulative voting rights, which means that the holders of more than 50% of the shares outstanding voting for the election of directors can elect 100% of the directors if the holders choose to do so, and, in that event, the holders of the remaining shares will not be able to elect any person or persons to the Board of Directors.

The Fund's By-Laws provide the holders of one-third of the outstanding shares of the Fund present at a meeting in person or by proxy will constitute a quorum for the transaction of business at all meetings, except that the Articles of Incorporation provide that a meeting to consider an amendment to the Fund's fundamental investment policies of investing in securities that would qualify an investment in the Fund as a "tax exempt bond" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax, 90% of the outstanding shares of the Fund must be present in person or by proxy to constitute a quorum for this particular purpose.

DIVIDENDS AND DISTRIBUTIONS

The Fund declares dividends equal to all its net investment income (excluding capital gains and losses, if any, and amortization of market discount) on each Fund Business Day and pays dividends on the last day of each month or, if the last day is not a Fund Business Day, on the preceding Fund Business Day. There is no fixed dividend rate. In computing these dividends, interest earned and expenses are accrued daily.

Net realized capital gains, if any, are distributed annually within 45 days after the end of the Fund's fiscal year.

All dividends and distributions of capital gains are automatically invested in additional Fund shares immediately upon payment thereof unless a shareholder has elected by written notice to the Fund to receive either of such distributions in cash.

HOW TO PURCHASE AND REDEEM SHARES

The Fund sells and redeems its shares on a continuing basis at net asset value and does not impose a sales charge for either sales or redemptions. All transactions in Fund shares are effected through the Fund's transfer agent which accepts orders for purchases and redemptions. There is no minimum initial investment, nor is there a minimum subsequent investment.

In order to maximize earnings on its portfolio, the Fund normally has its assets as fully invested as is practicable. Many securities in which the Fund invests require immediate settlement in funds of Federal Reserve member banks on deposit at a Federal Reserve bank (commonly known as "Federal Funds"). Accordingly, the Fund does not accept a subscription or invest an investor's payment in portfolio securities until the payment is converted into Federal Funds.

Shares will be purchased as of the first determination of the Fund's net asset value per share made after acceptance of the investor's subscription.

The Fund reserves the right to reject any subscription for its shares.

Shares are issued as of 12 noon, New York City time, on any Fund Business Day on which an order for the shares and accompanying Federal Funds are received by the Fund's transfer agent before 12 noon. Orders accompanied by Federal Funds and received after 12 noon on a Fund Business Day will not result in share issuance until the following Fund Business Day. In the case of Qualified Investors, orders received by the Fund's transfer agent before 12 noon, New York City time, on a Fund Business Day, without accompanying Federal Funds will result in the issuance of shares on that day provided that the Federal Funds required in connection with the orders are received by the Fund's transfer agent before 4:00 P.M., New York City time, on that day. Orders for which Federal Funds are received after 4:00 P.M., New York City time, will not result in share issuance until the following Fund Business Day. Fund shares begin accruing income on the day on which shares are issued to an investor.

There is no redemption charge, no minimum period of investment, and no restriction on frequency of withdrawals. Proceeds of redemptions are paid in cash. If a shareholder elects to redeem all the shares of the Fund he owns, all dividends accrued to the date of redemption are paid to the shareholder in addition to the proceeds of the redemption.

The right of redemption may not be suspended, or the date of payment upon redemption postponed, for more than seven days after shares are tendered for redemption, and the right of redemption may not be suspended, except for any period during which the New York Stock Exchange, Inc. is closed (other than customary weekend and holiday closings) or during which the Securities and Exchange Commission determines that trading thereon is restricted, or for any period during which an emergency (as determined by the Securities and Exchange Commission) exists as a result of which disposal by the Fund of its securities is not reasonably practicable or as a result of which it is not reasonably practicable for the Fund fairly to determine the value of its net assets, or for such other period as the Securities and Exchange Commission may by order permit for the protection of the shareholders of the Fund.

Redemption requests received by the Fund's transfer agent before 12 noon, New York City time, on any Fund Business Day become effective at the net asset value per share determined at 12 noon that day. Shares redeemed are not entitled to participate in dividends declared on the day a redemption becomes effective. Redemption requests received after 12 noon will result in a share redemption on the following Fund Business Day.

The Fund has reserved the right to redeem the shares of any shareholder if the net asset value of all the remaining shares in the shareholder's account after a withdrawal is less than $1,000 solely because of withdrawals from the account and not because of fluctuation in the value of the account. Written notice of a proposed mandatory redemption will be given at least 30 days in advance to any shareholder whose account is to be redeemed. During the notice period a shareholder who receives such a notice may avoid mandatory redemption by purchasing sufficient additional shares to increase his total net asset value to at least $1,000.

The redemption of shares may result in the investor's receipt of more or less than he paid for his shares and, thus, in a taxable gain or loss to the investor.

Direct Purchase and Redemption Procedures

Investors who wish to invest in the Fund may obtain a current prospectus and the subscription order form necessary to open an account by telephoning Reich & Tang L.P. at the following number:

(toll free) 800-221-3079

All shareholders will receive from the Fund confirmations of each individual purchase and redemption of Fund shares and a monthly statement listing the total number of Fund shares owned as of the statement closing date, purchases and redemptions of Fund shares during the month covered by the statement and the dividends paid on Fund shares of each shareholder during the statement period (including dividends reinvested in additional Fund shares).

Initial Purchase of Shares

Mail

Investors may send a check made payable to the Fund along with a completed subscription order form to:

Tax Exempt Proceeds Fund ,Inc.
c/o Reich & Tang L.P.
100 Park Avenue - 28th Floor
New York, New York 10017

Checks are accepted subject to collection at full value. Payment by a check drawn on any member of the Federal Reserve System can normally be converted into Federal Funds within two business days after receipt of the check. Checks drawn on a non-member bank may take substantially longer to convert into Federal Funds. An investor's subscription will not be accepted until the Fund receives Federal Funds.

Bank Wire

To purchase shares of the Fund using the wire system for transmittal of money among banks, investors should first telephone the Fund to obtain a new account number. The investors should then instruct a member commercial bank to wire their money immediately to:

The Bank of New York
Funds Processing Department
For Tax Exempt Proceeds Fund, Inc.
New account of (investor's name, address and account number) ________________
Tax ID # ________________________

The investor should then promptly complete and mail the subscription order form.

Investors planning to wire funds should instruct their bank early in the day so the wire transfer can be accomplished the same day. There may be a charge by the investor's bank for transmitting the money by bank wire, and there also may be a charge for use of Federal Funds. The Fund does not charge investors in the Fund for its receipt of wire transfers. Payment in the form of a "bank wire" received prior to 12 noon, New York City time, on a Fund Business Day will be treated as a Federal Funds payment received on that day.

Subsequent Purchases of Shares

Subsequent purchases can be made by mailing a check, by personal delivery or by bank wire as indicated above. There is no minimum for subsequent purchases of shares. All payments should clearly indicate the shareholder's account number.

Provided that the information on the subscription form on file with the Fund is still applicable, a shareholder may reopen an account without filing a new subscription order form at any time during the year the shareholder's account is closed or during the following calendar year.

Redemption of Shares

A redemption is effected immediately following, and at a price determined in accordance with, the next determination of net asset value per share following acceptance by the Fund's transfer agent of the redemption order (and any supporting documentation which it may require). Normally, payment for redeemed shares is made on the same Fund Business Day after the redemption is effected, provided the redemption request is received prior to 12 noon, New York City time. However, redemption payments will not be made until 15 days after the check (including a certified or cashier's check) used to purchase the shares has been deposited by the Fund.

A shareholder's original subscription order form permits the shareholder to redeem by written request and to elect redemption by check writing. A shareholder may only change the instructions indicated on his original subscription order form by transmitting a written direction to the Fund's transfer agent. Requests to institute or change any of the additional redemption procedures will require a signature guarantee.

When a signature guarantee is called for, the shareholder should have "Signature Guaranteed" stamped under his signature and signed at a member organization of a national stock exchange or a commercial bank or trust company in New York City (or any local commercial bank or trust company having a correspondent in New York City).

Written Requests

Shareholders may make a redemption in any amount by sending a written request addressed to:

Tax Exempt Proceeds Fund, Inc.
c/o Reich & Tang L.P.
100 Park Avenue - 28th Floor
New York, New York 10017

Normally the redemption proceeds are paid by check mailed to the shareholder of record.

Checks

By making the appropriate election on their subscription form, shareholders who are United States residents may request a supply of checks which may be used to effect redemptions. The checks, which will be issued in the shareholder's name, are drawn on a special account maintained by the Fund with the Fund's transfer agent. For Qualified Investors, checks will be pre-printed with a legend certifying compliance with specific limitations for withdrawal. Checks may be drawn in any amount. When a check is presented to the Fund's transfer agent for payment, the Fund's transfer agent, as agent for the shareholder, redeems a sufficient number of full and fractional shares in the shareholder's account to cover the amount of the check. The use of a check to make a withdrawal enables a shareholder in the Fund to receive dividends on the shares to be redeemed through the Fund Business Day on which the check clears. Checks provided by the Fund may not be certified. Fund shares purchased by check may not be redeemed by check within 15 days following the date of purchase.

There is no charge to the shareholder for checks provided by the Fund. The Fund reserves the right to impose a charge or impose a different minimum check amount in the future, if the Board of Directors determines that doing so is in the best interests of the Fund and its shareholders.

Shareholders electing the checking option are subject to the procedures, rules and regulations of the Fund's transfer agent governing checking accounts. Checks drawn on a jointly owned account may, at the shareholder's election, require only one signature. The Fund's transfer agent will not honor checks which are in amounts exceeding the value of the shareholder's account at the time the check is presented for payment. Since the dollar value of the account changes daily, the total value of the account may not be determined in advance and the account may not be entirely redeemed by check. The Fund reserves the right to terminate or modify the check redemption procedure at any time.

Investors wishing to avail themselves of this method of redemption should elect it on their subscription order form.

Qualified Investors making this election, are required to complete a certified resolution or other evidence of authorization in accordance with the Fund's transfer agent's normal practices. Appropriate authorization forms will be sent by the Fund's transfer agent to shareholders who select this option. As soon as the authorization forms are filed in good order with the Fund's transfer agent, it will provide the shareholder with a supply of checks. This checking service may be terminated or modified at any time.

DISTRIBUTION PLAN

Pursuant to Rule 12b-1 under the Investment Company Act of 1940, the Securities and Exchange Commission has required that an investment company which bears any direct or indirect expense of distributing its shares must do so only in accordance with a plan permitted by the Rule. The Fund's Board of Directors has adopted a distribution plan (the "Plan") and, pursuant to the Plan, the Fund and the Manager have entered into a Distribution Agreement with the Manager as distributor of the Fund's shares. There are no fees or expenses chargeable to the Fund under the Plan. The Fund's Board of Directors has adopted the Plan in case certain expenses of the Fund are deemed to constitute indirect payment by the Fund for distribution expenses. If a payment of fees under the Management Contract by the Fund to the Manager should be deemed to be indirect financing by the Fund of the distribution of its shares, such payments are authorized by the Plan.

Under the Distribution Agreement, the Manager, for nominal consideration and as agent for the Fund, will solicit orders for the purchase of the Fund's shares, provided that any subscriptions and orders will not be binding on the Fund until accepted by the Fund as principal.

The Plan provides that the Manager may make payments from time to time from its own resources, which may include the management fee and past profits for the following purposes: to defray the costs of, and to compensate others, with whom the Manager has entered into written agreements, for performing shareholder servicing and related administrative functions on behalf of the Fund; to compensate certain organizations for providing assistance in distributing the Fund's shares; to pay the costs of printing and distributing the Fund's prospectus to prospective investors; and to defray the cost of the preparation and printing of brochures and other promotional materials, mailings to prospective shareholders, advertising, and other promotional activities, including the salaries and/or commissions of sales personnel in connection with the distribution of the Fund's shares. The Manager, in its sole discretion, will determine the amount of such payments made pursuant to the Plan, provided that such payments will not increase the amount which the Fund is required to pay to the Manager for any fiscal year under the Management Contract in effect for that year.

FEDERAL INCOME TAXES

The Fund will elect to qualify under the Internal Revenue Code of 1986, as amended (the "Code"), as a regulated investment company that distributes "exempt-interest dividends" as defined in the Code. The Fund intends to continue to qualify for regulated investment company status. The Fund's policy is to distribute as dividends each year 100% (and in no event less than 90%) of its tax exempt interest income, net of certain deductions, and its investment company taxable income (if any). If distributions are made in this manner, dividends designated as derived from the interest earned on Municipal Obligations are "exempt-interest dividends" and are not subject to regular Federal income tax. Dividends paid from taxable income, if any, and distributions of any realized short-term capital gains (whether from tax exempt or taxable obligations) are taxable to taxable shareholders as ordinary income, whether received in cash or reinvested in additional shares of the Fund. The Fund does not expect to realize long-term capital gains and thus does not contemplate distributing "capital gain dividends" or having undistributed capital gain income within the meaning of the Code. The Fund will inform shareholders of the amount and nature of its income and gains in a written notice mailed to shareholders within 60 days after the close of the Fund's taxable year. The Tax Reform Act of 1986 (P.L. 99-514), as amended by the recently enacted Technical and Miscellaneous Revenue Act of 1988 (P.L. 100-647), ("TAMRA") affects many of the Federal tax aspects of Municipal Obligations and makes many important changes to the Federal income tax system, including a reduction in marginal tax rates, the elimination of the preferential treatment for capital gains and the elimination or reduction of many exclusions and deductions. In addition to these changes, P.L. 99-514 provides a unified state volume limitation for many types of tax exempt bonds and revises current arbitrage restrictions. Further, corporations will be required to include as an item of tax preference for purposes of the alternative minimum tax a portion of the amount by which its book income or earnings (including generally, tax exempt interest) exceeds its alternative minimum taxable income (determined without this tax preference item). Certain tax exempt interest is also included in the tax base for the additional corporate minimum tax imposed by the Superfund Amendments and Reauthorization Act of 1986.

With respect to the variable rate demand instruments, including participation certificates therein, the Fund has obtained and is relying on the opinion of bond counsel at the date of issuance or in the opinion of Battle Fowler, counsel to the Fund, that it will be treated for Federal income tax purposes as the owner thereof and the interest on the underlying Municipal Obligations will be tax exempt to the Fund. Counsel has pointed out that the Internal Revenue Service has announced in Revenue Procedure 83-55 that it will not ordinarily issue advance rulings on the question of ownership of securities or participation interests therein subject to a put and could reach a conclusion different from that reached by counsel.

If an issuer of a State or local tax exempt bond invests the proceeds of the bond issue in any "tax exempt bond", the income on which is not an item of tax preference and not includible in the alternative minimum tax computation for individual taxpayers, such issuer is not subject to the rebate provisions of Code Section 148 as amended by TAMRA. The rebate provisions would require an issuer that invests the bond proceeds in "higher yielding investments" (other than in "tax exempt bonds") to rebate a portion of the income from such investments, in order for the bond income to remain tax exempt to the bondholders. A "tax exempt bond" is any bond the income on which is excluded from gross income.

Internal Revenue Service Notice 87-22 provides that State and local bond issuers are exempt from the rebate requirements even if the bond proceeds are invested in tax exempt bonds indirectly through a qualified regulated investment company, that is, a corporation (a) that (i) meets the regulated investment company requirements of Section 852(a) of the Code, (ii) has one class of authorized and outstanding stock, and (iii) to the extent practicable invests all its assets in tax exempt bonds, and (b) 98% of the income of which is attributable to, or 98% of the weighted average of the assets of which are, tax exempt bonds. Notice 87-22 may be relied on until proposed regulations are issued. To date no proposed regulations have been issued although it is expected that such regulations will be consistent with the Notice.

Since the Fund is established primarily for issuers of tax exempt bonds that do not wish to be subject to the Code's rebate requirements, the Fund intends to comply with the provisions of Notice 87-22 and will invest only in tax exempt bonds the income from which, in the opinion of bond counsel at the date of issuance or in the opinion of Battle Fowler, counsel to the Fund, is not subject to the individual alternative minimum tax provisions.

The exemption of interest income for Federal income tax purposes does not necessarily result in an exemption under the income or other tax laws of any state or local taxing authority. Shareholders of the Fund may be exempt from state and local taxes on distributions of tax exempt interest income derived from obligations of the state and/or municipalities of the state in which they may reside but may be subject to tax on income derived from obligations of other jurisdictions. Shareholders should consult their own tax advisors about the status of distributions from the Fund in their own states and localities.

GENERAL INFORMATION

The Fund was incorporated under the laws of the State of Maryland on November 18, 1988 and it is registered with the Securities and Exchange Commission as a diversified, open-end, investment company.

The Fund prepares semi-annual unaudited and annual audited reports which include a list of investment securities held by the Fund and which are sent to shareholders.

For further information with respect to the Fund and the shares offered hereby, reference is made to the Fund's registration statement filed with the Securities and Exchange Commission, including the exhibits thereto. The Registration Statement and the exhibits thereto may be examined at the Commission and copies thereof may be obtained upon payment of certain duplicating fees.

NET ASSET VALUE

The net asset value of the Fund's shares is determined as of 12 noon, New York City time, on each Fund Business Day. Fund Business Day means weekdays (Monday through Friday) except customary national business holidays and Good Friday. It is computed by dividing the value of the Fund's net assets (i.e., the value of its securities and other assets less its liabilities, including expenses payable or accrued but excluding capital stock and surplus) by the total number of shares outstanding.

The Fund's portfolio securities are valued at their amortized cost in compliance with the provisions of Rule 2a-7 under the Investment Company Act of 1940. Amortized cost valuation involves valuing an instrument at its cost and thereafter assuming a constant amortization to maturity of any discount or premium, except that if fluctuating interest rates cause the market value of the Fund's portfolio to deviate more than 1/2 of 1% from the value determined on the basis of amortized cost, the Board of Directors will consider whether any action should be initiated. Although the amortized cost method provides certainty in valuation, it may result in periods during which the value of an instrument is higher or lower than the price an investment company would receive if the instrument were sold. The Fund intends to maintain a stable net asset value at $1.00 per share although there can be no assurance that this will be achieved.

CUSTODIAN, TRANSFER AGENT AND DIVIDEND AGENT

The Bank of New York is the custodian for the Fund's cash and securities and the is the transfer agent and dividend agent for the shares of the Fund. The bank does not assist in, and is not responsible for, investment decisions involving assets of the Fund.

FRANCISCO L. BORGES
TREASURER

State of Connecticut
OFFICE OF THE TREASURER

EDWARD J. FORAND JR.
DEPUTY TREASURER

GENERAL MEMORANDUM

November 30, 1988

TO: Honorable J. William Burns
Commissioner
Department of Transportation
P.O. Drawer A
24 Wolcott Hill Road
Wethersfield, CT 06109

FROM: Francisco L. Borges, State Treasurer
J. Edward Caldwell, State Comptroller
Anthony V. Milano, Secretary, OPM

SUBJECT: Implementation of Public Act 88-258, an Act Concerning the Establishment of a Tax-Exempt Bond Proceeds Fund (TEBPF)

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I. Example of Project Identification - Housing
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20 Trinity Street Hartford, Connecticut 06106
An Equal Opportunity Employer

I. THE TAX-EXEMPT BOND PROCEEDS FUND

Public Act 88-258 authorizes the Treasurer to establish a tax-exempt mutual fund for the investment of state bond proceeds. This legislation was enacted to meet provisions of the Tax Reform Act of 1986.

Stated simply, for programs and projects which pass through the proceeds of tax-exempt bonds, the Tax Reform Act defined "expenditure" as the point at which the ultimate recipient makes a payment to a contractor or vendor. Until such "expenditure" is made, funds must be invested. The State, as the bond issuer, must track those thousands of investment streams even though it no longer has direct control of the funds, must compare the earnings back to the rate of interest on the underlying bonds, and must "rebate" excess earnings to the federal government, even if those earnings were received by others. Potential payments of a portion of such earnings would be due the federal government, even if this investment was only overnight.

The level of tracking required is simply not feasible. The Tax-Exempt Bond Proceeds Fund (TEBPF) is a permitted alternative, provided all pass-throughs of tax-exempt bond proceeds are invested therein.

Up to now, as an interim step to keep your programs in operation, the State has been fronting all pass-through projects with cash from other sources since the effective date of the Tax Reform Act of 1986. It is no longer possible to do so. Immediate start-up of the TEBPF so that bonds may again be issued for your programs is a matter of some urgency. The TEBPF must commence operations by January 1, 1989.

The purposes of this memorandum are as follows:

- To inform State agencies about the TEBPF and the urgency of its establishment
- To explain the new project identification system that all agencies will need to use for projects that are directed through the mutual fund and ultimately will be used to identify all capital projects funded from bond proceeds.
- To describe fully the operating characteristics and requirements of the TEBPF

II. BASIC TEBPF REQUIREMENTS

Payments from State tax-exempt bond proceeds, regardless of the date of approval or allotment, made for grant or loan programs of the state must be deposited into TEBPF beginning January 1, 1989.

The monies deposited may be withdrawn by the grantee/loan recipient when they are needed to meet an expenditure for a project or to refund the unexpended portion of the grant back to the state.

The following is a brief listing of questions typically asked about how this mutual fund will be set-up and what agencies must do to comply with these requirements.

- Participants: Who must participate in the tax-exempt mutual fund?

All State agencies which administer grants and certain loans financed from tax-exempt bond proceeds. These grants or loans are to municipalities, other public agencies or 501(c)(3) tax-exempt organizations.

- Tax-Exempt vs. Taxable: How does an agency know whether or not the grant-in-aid or loan is taxable or tax-exempt?

Prospectively, agencies must fill out a tax questionnaire and submit that information to OPM. OPM will tentatively classify each project as either "governmental" or "private activity" and this information will appear on the State Bond Commission agenda item. To the extent possible, entire programs will either be included in the TEBPF or not be included.

For both projects in progress and future projects, OPM and the Treasurer's Office will work with you to determine which must be included in the fund. See Part III and Part IV, below.

- Programs administered on a reimbursement basis: What if your grant program is administered on a reimbursement basis? Does it still have to go through the mutual fund?

Yes. Programs which operate on a reimbursement basis will be included initially in order to reduce the likelihood of error.

- o Timing of payments through the TEBPF: Does it make any difference that the State Bond Commission approved the grant five years ago?

All payments made after January 1, 1989 from tax-exempt bond proceeds must go through the mutual fund, no matter when approved or allotted.

- o Payments to program recipients: How do program recipients receive and make payment?

Through the procedures outlined below, at the point in the payment sequence when a check would have gone out from the State Comptroller's Office to the recipient, a deposit will instead be made in the recipient's name in the TEBPF. The recipient will be issued checks against that account. The checks will be honored only if the "Recipient," "Project Name," and "Project No." blanks have been filled in and the appropriate one of two certifications printed on the face of the check has been properly filled out. The first certification applies to any payment for which a municipality has not already advanced its own funds. The certification indicates that the check is being issued for a payment to a contractor/vendor for the purpose for which the funds were granted. Contractor/vendor generally means any payee other than the recipient.

If the check is made payable to the recipient in the case of a reimbursement, the recipient must certify that the payment is a reimbursement and must indicate the date of payment and source of funds being reimbursed. Withdrawals from TEBPF made payable to the recipient should be audited by your agency against proof of expenditure.

Checks which are made out to a recipient, but for which the first rather than the second certification has been completed will not be honored.

- O Sequence of events that lead to payment: What will happen when a payment request is made to the Comptroller's Office for a program recipient?

    1. The State Comptroller's Office will post project funds electronically for grant recipient payments (no check required).

    2. The State Treasurer will transfer project funds via electronic funds transfer to the (TEBPF) fund manager (Reich & Tang).

3. The deposit of the project funds will be made by Reich & Tang to the recipients TEBPF account.

4. Reich & Tang will honor all requests for payments made by the program recipient to contractors or vendors upon completion of certification printed on the face of the check.

III. DEFINITION OF "PROJECT" FOR PURPOSES OF THE TEBPF AND THE OPM CAPITAL BUDGET SYSTEM

Payments under a grant or loan program made from tax-exempt bond proceeds deposited into TEBPF must have identification. Identification will be made on a project by project basis. Treasury, the Comptroller's Office and OPM will work with agencies to define the projects.

A project is defined as having:

1. The same tax classification (as determined from the tax questionnaire)
2. The same administering State agency
3. The same recipient signatory authorization

Example:

A "project": grants for rehabilitation of various housing developments (generally "governmental") to the Hartford Housing Authority (a single recipient and signatory) made by the Department of Housing (a single administering State agency).

A "project": school construction grants (generally "governmental") to the City of Hartford (a single recipient signatory) for work at Hartford Public High School and Bulkeley High School.

Not a "project": grants to the Hartford Housing Authority and the New Haven Housing Authority (different recipient signatories) by the Department of Housing for rehabilitation of various housing developments

Not a "project": grants to the Hartford Housing Authority and the City of Hartford (differing signatory authorities) for asbestos removal.

IV. PROJECT NUMBERING

The numbering system which is being established for the TEBPF will be used for all State of Connecticut bond projects once the OPM Capital Budgeting System is established. The project numbering system will be as follows:

A. Agencies must maintain the existing numbering system using the bond fund, agency, SID, and project number. A new project ID system, in addition to the existing system, should be recorded on Line 2 after the name of the payee.

B. Agencies must use the 80,000 batch series to identify for the Comptroller and Treasurer the payments to the tax-exempt mutual fund.

C. Project ID must be recorded on the TEBPF Journal and will be a 10 digit numerical sequence as follows:

1. First four digits - the agency number
2. The next two digits - the program code
3. The next four digits - the project number

Please note that within the definition of a project each project number must be unique to that particular project. This unique project number must be maintained for that project and only that project, including any supplemental funding.

D. The following instructions are intended as a guide to assist agencies in coding of capital projects and is divided into two numbering sequences as follows: 1) State grants-in-aid, advances-in-aid, and loan programs; and 2) State construction/acquisition projects.

1. State Grants-In-Aid, Advances and Loans:

    a. An agency must use the first four digits in the ten digit project ID for the agency number. This agency code should be one unique agency number.

    b. The next two digits should be used by an agency to identify major programs. An agency should use a two digit numbering system starting with 01 through 49.

c. The next four digits must be used by an agency to identify specific projects within a program. The project numbers will be within the range from 0001 to 9999.

d. Also, lump sum requests should be coded using the program "00," and project code "0000."

Please note that these numbers are unique to a project, and must be maintained through all project phases, i.e., land acquisition, design and construction including any supplemental funding. An example of how a project ID could be developed for the Department of Housing is given in Attachment I, and an example for the Department of Education is given in Attachment II.

2. State Construction Projects:

Once the OPM Capital Budget System is implemented, agencies will be required to code all capital projects in accordance with the new ten digit project identification code. The assignment of project ID codes will be detailed in future directives.

V. PROCEDURE FOR ESTABLISHMENT OF PROJECT NUMBERING FOR ALL GRANT AND LOAN PROGRAMS

The procedure will be as follows:

A. With advice and consultation from OPM, agencies must prepare the following forms:

1. "Listing of Programs to be Funded with Tax-Exempt Bond Proceeds to be Deposited in the Tax-Exempt Bond Proceeds Fund" (Attachment III)

2. "Listing of Programs that Will Not Be Deposited in the Tax-Exempt Bond Proceeds Fund" (Attachment IV).

All of your agency's bond-funded grant and loan programs must be included on one of the two forms. The Agency Head must sign and date these forms and submit copies to OPM, Office of the Treasurer, and Office of the Comptroller, Accounting Systems Division, by December 5, 1988.

B. For all projects and programs that will be included in the Tax-Exempt Mutual Fund program, each agency should assign project numbers, list them on the "Grant/Loan Project Identification Number Assignment" form (Attachment V) and submit the forms to OPM for review. (Agencies should retain a copy for their records). The forms must be received by OPM by December 15, 1988.

C. OPM will review the forms and will contact the agency within five working days, as follows:

If approved:

OPM signs and dates the form, makes copies, and distributes as follows:

1 copy to Treasurer
1 copy to the Agency
1 copy for OPM files

If unapproved:

OPM will contact the agency by phone to resolve any problems.

Possible problems include:

- Incorrect categorization of program
- Incorrect or inconsistent definition of project (e.g. more than one grant recipient covered in single project)
- Duplicate project numbers

D. The Treasurer will not activate a TEBPF account or process payments for any project for which there has not been an approved Project Number.

VI. ESTABLISHMENT OF PROJECT ACCOUNTS

The firm of Reich and Tang has been hired to manage the TEBPF. The fund manager will establish project accounts within TEBPF for each grant/loan recipient.

Reich and Tang, using the approved listing established in accordance with Part V, will work with project recipients to set up their accounts. A new account letter used to establish withdrawal authorization will be completed and signed by project recipients. A new account letter must be completed for each project by the grant/loan recipient. The grantee agency must provide a new account letter to the recipient for completion. The recipient will transmit this new account letter to Reich and Tang.

VII. PAYMENT PROCEDURE

A. IDENTIFICATION

1. TEBPF payments must be processed in separate expenditure batches.

2. The batch number must begin with the 80,000 series and be initialized each fiscal year. Payee information on the batch, CO-19, should read:

   "TAX-EXEMPT BOND PROCEEDS FUND WIRE DEPOSIT - NO CHECK REQUIRED"

   The amount should be the total for all payees listed. Listing of individual payees on the CO-19 is not required. The batch should be stamped in the upper right hand corner - "TEBPF"

3. A TEBPF Journal (Attachment VI) is to be completed. This journal provides information as to deposit project account numbers and amounts. The attached sample may be copied for use until a supply of printed forms is available.

4. Payee information on the CO-17 or CO-17L should appear as follows:

   NAME - line 1: Town of __________, if a town,
   or payee name
   line 2: ACCT. # XXXX-XX-XXXX (agency number-program number-project number, i.e. the project identifier code)

   ADDRESS - MUST be left blank

   Complete all other payee information as required in the Expenditure Section of the State Accounting Manual (SAM).

B. TRANSMITTAL

1. To the Comptroller - Special payment batches, for TEBPF (Attachment VII), numbered in the 80,000 series, will be sent to the Central Accounts Payable Division (CAP) of the Comptroller's Office

for payment processing.

2. To the Treasurer - AT the same time as a payment batch is forwarded to CAP, the Treasurer's copy of the TEBPF journal will be sent to:

   The Office of the State Treasurer
   20 Trinity Street
   Hartford, CT

   ATT: TEBPF Coordinator

C. CORRECTIONS AND ADJUSTMENTS

1. Improperly identified accounts -

   Payment made for deposit into TEBPF that are not properly identified or do not have an account set up with the fund manager will require corrective action by the agency originating the claim. Telephone contact will be made by the TEBPF manager concerning improperly identified payments.

   Subsequently, a TEBPF journal noting correction and the date of the correction should be forwarded to Treasury. An area has been provided for corrections on the TEBPF journal.

   In the event that a State payment is deposited into TEBPF in error, and the agency is notified by Reich & Tang that an account does not exist for the project, the following procedure should be followed:

   a)Reich and Tang will deposit unidentified payments into a State account awaiting advice of disposition from the agency.

   b) The agency should request a refund of expenditure by wire deposit from the TEBPF by:

      1. Completing a TEBPF correction journal indicating that a deposit was made to TEBPF in error. An explanation must be given for the reason the payment was made to the TEBPF. Certification by the agency is required on all corrections made to TEBPF deposits. The batch number on the TEBPF correction journal should be the original batch number, a dash and a sequential number

beginning with 1 for the first adjustment on a batch (example Batch 80,005-1).

2. Filling out a deposit slip, CO-39, following procedures prescribed in the SAM Coding Section, paragraph 2.2.3, Refunds of Expenditures - other than Budgeted Appropriations.

3. Submitting both documents, the TEBPF correction journal and the CO-39, to Treasury, TEBPF Coordinator.

4. Upon completion of the wire deposit, a receipted CO-39 will be returned to the agency as advice of refund of the TEBPF deposit error.

2. Misdirected payments -

If the agency fails to properly identify the payment batch as a tax-exempt mutual fund payment and a check is mailed to the recipient in error, the recipient must return the undeposited check to → the agency. The agency must then follow procedures as prescribed in the State Accounting Manual, Expenditure Section, Vendor Check Cancellation Procedure.

Agency
Voids a
Form CO790
+
than prepares
new payment List
in 84,000 Series

3. Improperly deposited payments -

a. Money deposited to an incorrect project number - an adjustment can be made on the TEBPF journal, within the correction area. Both the correct and incorrect information must be reported. The incorrect amount should be enclosed in parenthesis. See section C-1 for an explanation of batch numbering.

b. Money deposited incorrectly to TEBPF - effect recovery from the recipient by check made payable to the State. Follow the procedures as prescribed in SAM for refund of expenditures.

c. Deposit amount incorrect:

i Amount greater than - effect recovery from payee directly using the already-established procedures for refund of expenditures

ii Amount less than - issue an additional payment for the difference (on an 80,000 batch)

iii Amount differs between projects - follow the rules established in (c)-i and (c)-ii above.

D. RECONCILIATION

It is recommended that expenditures paid to grantees and loan recipients for deposit into TEBPF be reconciled with the periodic statements provided by the TEBPF fund manager. Boxes 7 & 8 and the blank column between boxes 12 & 13 of the TEBPF journal have been included to allow for reconciliation.

Errors discovered during reconciliation should be reported to the Treasurer utilizing the TEBPF journal in the area provided for corrections.

VIII. NONCOMPLIANCE WITH TEBPF REQUIREMENTS

If through an error, a recipient receives funds directly and fails to comply with the state's deposit requirement for tax-exempt bond fund grant-in-aid program monies, the recipient will be in violation of State law and all State grant/loan awards may be in jeopardy.

The continued tax-exempt status of all State of Connecticut bond issuance depends upon the successful implementation of the TEBPF. If a pattern develops in which a State agency has not done what is required to assure that all of its payments to grant and loan recipients from tax-exempt bond proceeds flow through the TEBPF, all such payments by that agency may be halted until correction is made.

IX. MODIFICATION OF GRANT AND LOAN CONTRACTS

In order to assure that the fund will operate in a way which permits the bond counsel to approve the issue of bonds as tax-exempt, a modification to new grant and loan contracts paid with tax-exempt bond proceeds will need to be implemented.

Guidelines will be issued at a later date to clarify this issue. However, please keep in mind that new tax-exempt bond fund grant-in-aid program contracts must require that:

A. Qualifying grant and loan money be invested in TEBPF.

B. The proceeds from the bonds only be withdrawn from a TEBPF account for a contractor or vendor payment and not be reinvested after release from TEBPF, unless the payment is a reimbursement. If a reimbursement, proof of expenditure (generally a cancelled check) must be provided to the State Agency.

C. Fund withdrawal requests be accompanied by a signed certification that the moneys will be used immediately for project expenditure.

D. Unexpended funds be returned to the State.

X. GENERAL

Best efforts have been made to define the procedures that will fit in all cases. However, there may be exceptions to be dealt with and your cooperation and forbearance will be necessary in the start up process.

Questions may be directed as follows:

PROJECT CLASSIFICATION OR BOND COUNSEL ISSUES:

Office of the State Treasurer, TEBPF Coordinator - 566-5054
Office of Policy and Management, Capital Program Unit
566-4757

PAYMENT PROCEDURE:

Office of the State Comptroller, Central Accounts Payable,
Special Handling Section - 566-3895

TEBPF ACCOUNT INFORMATION:

Fund Manager, Reich & Tang - 1-800-221-3079

ATTACHMENT I
DEPARTMENT OF HOUSING

Step 1

Determine the agency number 1150

Step 2

List the major grant/advance/loan programs and assign a unique program code for all bond financed programs starting with code 01 as follows:

Program Description		Agency - Code
1)	Grants for innovative housing for the homeless	1155 - 01
2)	Grants/loans for Moderate Rental Housing Rehabilitation	1155 - 02
3)	Grants for Affordable Housing	1155 - 03
4)	Housing Purchase and Rehabilitation	1155 - 04
5)	Grants/Loans for Congregate Elderly Housing	1155 - 05
6)	Grants/Loans for Rental Housing for the Elderly	1155 - 06
7)	Grants for Community Development/ Neighborhood Rehabilitation	1155 - 07
8)	Grants/Loans for Limited Equity Cooperatives	1155 - 08
9)	Grants/Loans for Mutual Housing	1155 - 09
10)	Grants for Housing Site Development	1155 - 10
11)	Loans/Advances to Community Housing Development Corporations	1155 - 11
12)	Grants for Land Bank and Land Trust	1155 - 12
13)	Loans/Advances for Urban Homesteading	1155 - 13
14)	Energy Conservation Loan Programs	1155 - 14
15)	Grants to Public Housing Authorities for removal of Hazardous Material	1155 - 15
16)	Loans for Removal of Hazardous Materials	1155 - 16
17)	Grants-Loans to Senior Citizens for Homeowner Emergency Repairs	1155 - 17
18)	Lump sum for all housing purposes	1155 - 00

Step 3

Determine how specific projects will be coded within program categories using the number sequence 0001 through 9999. Please note that this specific project ID must not exceed 9999. It is important to make sure that the definition of a project is maintained at the proper level in order to not exceed the number 9999.

Example

A) An elderly housing grant-in-aid to New Haven
Project ID - 1155-06-0001

B) An affordable housing grant to Hartford
Project ID - 1155-03-0001

10

ATTACHMENT II
DEPARTMENT OF EDUCATION

Step 1

Determine the agency number - 7001

Step 2

List the major grant programs and assign a unique program code for all bond financed programs starting with code 01 as follows:

Project Description	Agency - Code
1) Grants-in-aid for local school building projects	7001 - 01
2) Grants-in-aid for vocational education equipment	7001 - 02
3) Projects for CPTV	7001 - 03

Step 3

Determine how specific projects will be coded within program categories using the number sequence 0001 through 9999. Please note that this specific project ID must not exceed 9999. It is important to make sure that the definition of a project is maintained at the proper level in order to not exceed the number 9999.

Example

A) A school building project in Hartford that is determined to be a governmental purpose in accordance with the 1986 Tax Reform Act.
Project ID - 7001-01-0641

B) A grant for vocational education equipment to Hartford that is determined to be governmental.
Project ID - 7001-02-0641

LISTING OF PROGRAMS TO BE FUNDED WITH TAX-EXEMPT BOND PROCEEDS TO BE DEPOSITED IN THE TAX-EXEMPT BOND PROCEEDS FUND IN ACCORDANCE WITH PUBLIC ACT 88-258

Agency Name: ______________ Contact Person: ______________ Phone ______________

Agency/Program No.	Program Description	Comments

____
DATE

____
Approved by Agency Head

Instructions: This form should be used to establish program accounts for the Tax-Exempt Bond Proceeds Fund. Please submit the original to OPM with copies to the State Treasurer and the State Comptroller. NOTE: An Agency should use only one agency number.

LISTING OF PROGRAMS THAT WILL NOT BE DEPOSITED IN THE TAX-EXEMPT BOND PROCEEDS FUND

Agency Name: ____________________ **Contact Person:** ____________________ **Phone:** ____________

Agency/Program No.	Program Description	Justification for Exemption from

____
DATE

____
APPROVED BY AGENCY HEAD

INSTRUCTIONS: **This form should be used to list those programs that do not need to utilize the Tax-Exempt Bond Proceeds Fund.** An example would be any program whose payments derive from taxable bonds. If there is any doubt about the eligibility of a project for exemption from the Tax-Exempt Bond Proceeds Fund, it should be included in the TEBPF program. Please submit the original of this form to OPM with copies to the State Treasurer and the State Comptroller. NOTE: An Agency should use only one agency number.

GRANT/LOAN PROJECT IDENTIFICATION NUMBER ASSIGNMENT

Agency Name: ______________________ Contact Person: ______________________ Phone: ____________

Capital Project Noumber	Title/Name of Recipient	Statutory Reference	Bond Commission Agenda		Fund
			Date	Item #	

OPM APPROVAL:

BY: ______________________ DATE: ______________________

ATTACHMENT VI

TAX-EXEMPT BOND PROCEEDS FUND (TEBPF) DEPOSIT JOURNAL

NEW 11/[illegible]

STATE OF CONNECTICUT
OFFICE OF THE STATE TREASURER

(1) BATCH DATE	(2) BATCH NUMBER	(3) AGENCY NUMBER	(4) AGENCY TELEPHONE NO./CONTACT PERSON	(5) PAGE OF

(6) BATCH TOTAL	(7) DEPOSIT DATE (PER FUND MANAGER)	(8) TOTAL DEPOSITED (PER FUND MANAGER)

(9) AGENCY	(10) BOND FUND	(11) PAYEE / PROJECT NAME	(12) PROJECT NUMBER		(13) DEPOSIT AMOUNT	(14) EXPENDITURE PROJECT TOTAL	(15) ACT N/F
			(16) PAGE TOTAL				

CORRECTIONS

CERTIFICATION	AGENCY	TREASURY

DISTRIBUTION: PART 1 - TREASURER PART 2 - AGENCY

ATTACHMENT VI

FORM NAME: Tax-Exempt Bond Proceeds Fund (TEBPF)

PURPOSE: Submitted to Treasury at the same time as the Tax-Exempt Mutual Fund Expenditure Batch is submitted to the Comptroller's Office - Central Accounts Payable.

DISTRIBUTION: Agency, Treasury, Fax copy to TEBPF Fund Manager

COMPLETION INSTRUCTIONS:

Agency must complete blocks 1-6 and 9-16. All blocks are required except #15. This form must be completed and sent to the Treasurer's Office for reconciliation with the Comptroller's Office and the Fund Manager's statement.

X-REF NUMBER	MAX LENGTH	NAME/DESCRIPTION
1		BATCH DATE - Date agency transmitted to Comptroller's Central Accounts Payable.
2	5	BATCH NUMBER - Must be 80,000 series.
3	4	AGENCY NUMBER - Submitting Agency Number - Must be the same as original Expenditure batch.
4		AGENCY TELEPHONE NUMBER/CONTACT PERSON
5		PAGE OF - Page number out of total number of pages in this listing.
6	15	BATCH TOTAL - Dollar Amount of Batch.
7		DEPOSIT DATE (PER FUND MANAGER) - To be completed when reconciling fund statement - date monies deposited.
8	15	TOTAL DEPOSITED (PER FUND MANAGER) - To be completed when reconciling fund statement - should equal batch total.
9	4	AGENCY - Expending Agency Number
10	4	BOND FUND - Tax-Exempt Bond Appropriation Fund

ATTACHMENT VI

X-REF NUMBER	MAX LENGTH	NAME/DESCRIPTION
11		PAYEE/PROJECT NAME - List 2 lines - (double space after each payee) Line 1 - Town of xxxxx Line 2 - Project Name - May be a detailed description that will identify for the grantea/loan recipient the payment being made.
12	10	PROJECT NUMBER - Must be 10-digit project number per OPM's specifications.
13	15	DEPOSIT AMOUNT - Individual payee amount.
14	15	EXPENDITURE PROJECT TOTAL - Cumulative total.
15	1	ACT N/F - Action - New Account or Final Payment.
16	15	Page Total

[illegible]

ATTACHMENT VII

EXPENDITURE BATCH HEADER
CO-18 REV. 2/86
(Stock No. 6838-108-01)

STATE OF CONNECTICUT
OFFICE OF THE STATE COMPTROLLER

TO: Central Accounts Payable Division, 30 Trinity Street, Hartford, CT 06106

(1) AGENCY NO.	(2) BATCH NUMBER	(3) NO. OF DOC.	(4) BATCH AMOUNT
1155	80,000	1	300,000.00

(5) SUBMITTED BY (Agency Name): Dept. of Housing

(6) TELEPHONE NUMBER - BUSINESS OFFICE: x1234

(7) PAYEE	(8) PAYEE LIST ☐	(9) PURCHASE ORDER NUMBER	(10) REQ. FOR RES. OF FUNDS OR TRAV. AUTH. NO.	(11) AMOUNT OF INVOICE
TAX-EXEMPT BOND PROCEEDS FUND Deposit				300,000.00

NO
CHECK REQUIRED

(12) CHECK THE APPROPRIATE BOX ☐ TAPE ☐ ON-LINE ☒ CENTRALLY

AGENCY CERTIFICATION

As a duly authorized agent of the above named agency, I do hereby certify that to the best of my knowledge the amount shown above equals the total of the invoices and/or payrolls submitted herewith for payment and are valid claims against the State; no commission, bonus or reward has been promised or received or is expected on account thereof, by an officer or employee of the State; and the expenditures are authorized and properly chargeable to appropriations as indicated.

(13) AUTHORIZED SIGNATURE (Agency Head)	(14) CONTACT PERSON	(15) DATE

DISTRIBUTION: Original — Comptroller Part 2 — Agency

AMERICAN SILVER CITY MUSEUM
AMOS HOUSE INC
ANCIENT BURYING GROUND ASSOCIATION
ANDOVER, TOWN OF
ANSONIA HOUSING AUTHORITY
ANTIQUARIANS & LANDMARKS SOCIETY
APT FOUNDATION, THE
AREA COOPERATIVE EDUCATION SERVICE
ARTISTS COLLECTIVE INC
ASHFORD, TOWN OF
AVON, TOWN OF

BARKHAMSTED, TOWN OF
BEACON FALLS, TOWN OF
BERLIN, TOWN OF
BETHANY, TOWN OF
BETHSAIDA COMMUNITY (NORWALK)
BIBLIOMATION INC
BLOOMFIELD, TOWN OF
BOLTON, TOWN OF
BOOTH & DIMOCK MEMORIAL LIBRARY
BOYS VILLAGE YOUTH & FAMILY
BRANFORD DAY CARE
BRANFORD HOUSING AUTHORITY
BRANFORD, TOWN OF
BRIDGEPORT COMMUNITY HEALTH CENTER
BRIDGEPORT ECONOMIC DEVELOPMENT CORPORATION
BRIDGEPORT, CITY OF
BRISTOL EMERGENCY SHELTER & HOUSING COALITION
BRISTOL HOUSING SITE DEVELOPMENT AGENCY
BRISTOL, TOWN OF
BROAD PARK DEVELOPMENT CORPORATION
BROOKFIELD HOUSING AUTHORITY
BROOKFIELD, TOWN OF
BROOKLYN HOUSING AUTHORITY
BROOKLYN, TOWN OF
BUSHNELL PARK CAROUSEL SOCIETY INC

CANTERBURY, TOWN OF
CAPITAL REGION EDUCATION COUNCIL
CAPITAL REGIONAL LIBRARY COUNCIL
CENTRAL NAUGATUCK VALLEY HELP INC
CHARTER OAK TEMPLE RESTORATION ASSOC
CHEMICAL ABUSE SERVICES AGENCY
CHENEY HALL FOUNDATION INC
CHESIRE, TOWN OF
CHESTER, TOWN OF
CHILD & FAMILY AGENCY OF SOUTHEASTERN CT
CHILD GUIDANCE CENTER OF GREATER BRIDGEPORT
CHILD GUIDANCE CLINIC OF SOUTHEASTERN CT
CHILD GUIDANCE CLINIC OF WATERBURY
CHILDRENS' CENTER
CHILDRENS' HOME OF CROMWELL
CHURCH OF THE GOOD SHEPHERD

CLINTON HOUSING AUTHORITY
CLINTON, TOWN OF
COLCHESTER HOUSING AUTHORITY
COLCHESTER, TOWN OF
COLEBROOK, TOWN OF
COLUMBIA, TOWN OF
COLUMBUS HOUSE
COMMITTEE ON TRAINING AND EMPLOYMENT
COMMUNITY ACTION COMMITTEE OF DANBURY
COMMUNITY HEALTH AFFILIATES
COMMUNITY HEALTH CENTER
COMMUNITY LAND TRUST OF WINDHAM
COMMUNITY PROVIDER CONSORTIUM
COMMUNITY RENEWAL TEAM OF GREATER HARTFORD
COMPANY OF FIFERS & DRUMMERS
CONGREGATIONAL CHURCH OF THOMPSON
CONTINUUM OF CARE
COOPERATIVE EDUCATIONAL SERVICES
CORNWALL, TOWN OF
COVENTRY HISTORICAL SOCIETY INC
COVENTRY HOUSING AUTHORITY
COVENTRY, TOWN OF
CREATIVE HOUSING (HARTFORD) INC
CT ANTIQUE FIRE APPARATUS ASSOCIATION
CT CHILDREN' MUSEUM
CT ELECTRIC RAILWAY ASSOC
CT HALFWAY HOUSE
CT HISTORICAL SOCIETY
CT HOLDING ACCOUNT
CT JUNIOR REPUBLIC
CT NAUTILUS COMMITTEE
CT PUBLIC BROADCASTING
CT RENAISSANCE INC
CT RESOURCES RECOVERY AUTHORITY
CT STATE FIREMAN'S ASSOC
CT TRUST FOR HISTORIC PRESERVATION INC
CURTIS HOME INC

DANBURY HOUSING AUTHORITY
DANBURY, TOWN OF
DANIELSON, BOROUGH OF
DARIEN, TOWN OF
DEEP RIVER, TOWN OF
DERBY HOUSING AUTHORITY
DERBY, TOWN OF
DURHAM, TOWN OF

EAST CONN INC
EAST GRANBY, TOWN OF
EAST HADDAM, TOWN OF
EAST HAMPTON HOUSING AUTHORITY
EAST HAMPTON, TOWN OF
EAST HARTFORD HOUSING AUTHORITY
EAST HARTFORD, TOWN OF

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EAST HAVEN PUBLIC LIBRARY
EAST LYME, TOWN OF
EAST WINDSOR HOUSING AUTHORITY
EAST WINDSOR, TOWN OF
EASTER SEAL REHABILITATION CENTER OF GREATER WATERBURY
EASTFORD, TOWN OF
EDGERTON GARDEN CENTER INC
EDUCAITONAL RESOURCES INC
EL HOGAR DEL FUTURO
ELLINGTON, TOWN OF
ENFIELD HOUSING AUTHORITY
ENFIELD, TOWN OF
ESSEX, TOWN OF

FAIR HAVEN COMMUNITY HEALTH CLINIC
FAIRFIELD HOUSING AUTHORITY
FAIRFIELD HOUSING SITE DEVELOPMENT AGENCY
FAIRFIELD, TOWN OF
FARMINGTON VALLEY ARTS CENTER
FARMINGTON, TOWN OF
FATHER NADOLNY GOOD NEWS FUND
FRANKLIN, TOWN OF

GILBERT SCHOOL
GILEAD HOUSE
GOODSPEED OPERA HOUSE FOUNDATION
GOSHEN, TOWN OF
GRANBY HOMES FOR SENIOR CITIZENS
GRANBY HOUSING SITE DEVELOPMENT AGENCY
GRANBY, TOWN OF
GREATER NORWALK COMMUNITY COUNCIL
GREENWICH HOUSING AUTHORITY
GREENWICH, TOWN OF
GRISWOLD, TOWN OF
GROTON, TOWN OF
GUILFORD CENTER FOR CHILDREN
GUILFORD, TOWN OF

HALL NEIGHBORHOOD HOUSE
HALL NEIGHBORHOOD HOUSE INC
HAMDEN, TOWN OF
HAMPTON, TOWN OF
HARTFORD APARTMENT IMPROVEMENT PROGRAM
HARTFORD COALITION FOR EMERGENCY SHELTERS
HARWINTON, TOWN OF
HEBRON HOUSING AUTHORITY
HEBRON, TOWN OF
HMS ROSE FOUNDATION
HOUSATONIC REGIONAL RESOURCES RECOVERY AUTHORITY
HOUSE OF BREAD INC

INTERLUDE INC
INTERNATIONAL INSTITUTE OF CONNECTICUT

KEELER TAVERN MUSEUM
KEENEY CULTURAL CENTER
KENT, TOWN OF
KILLINGLY HOUSING AUTHORITY
KILLINGLY, TOWN OF

LAKE HOUSATONIC AUTHORITY
LAUREL HOUSE
LEDYARD, TOWN OF
LIBRARY EXCHANGE AIDS PATRONS
LIFE HAVEN INC
LISBON HISTORICAL SOCIETY
LITCHFIELD HOUSING AUTHORITY
LITCHFIELD, TOWN OF
LITTLE THEATRE OF MANCHESTER INC
LOCKWOOD-MATTHEWS MUSEUM OF NORWALK
LYME HISTORICAL SOCIETY
LYME, TOWN OF

MADISON, TOWN OF
MANCHESTER HOUSING AUTHORITY
MANCHESTER LAND TRUST
MANCHESTER, TOWN OF
MANSFIELD HOUSING AUTHORITY
MANSFIELD, TOWN OF
MARLBOROUGH, TOWN OF
MATTABASSETT DISTRICT
MC CALL FOUNDATION
MERIDEN HOUSING AUTHORITY
MERIDEN YWCA
MERIDEN, CITY OF
METROPOLITAN DISTRICT
MID-FAIRFIELD CHILD GUIDANCE CENTER
MIDDLEBURY, TOWN OF
MIDDLETOWN HOUSING AUTHORITY
MIDDLETOWN, TOWN OF
MILFORD HOUSING AUTHORITY
MILFORD, TOWN OF
MILITARY MUSEUM OF SOUTHERN NEW ENGLAND
MOHONK HOUSE
MONROE, TOWN OF
MONTEVILLE, TOWN OF
MORRIS FOUNDATION
MOUNT OLIVE CHILD DEVELOPMENT CENTER
MUSEUM OF AMERICAN THEATRE
MY SISTERS' PLACE INC
MYSTIC SEAPORT MUSEUM INC

NAUGATUCK HOUSING AUTHORITY
NAUGATUCK, BOROUGH OF
NEHEMIAH HOUSING CORPORATION
NEIGHBORHOOD HOUSING SERVICE OF NORWALK
NEIGHBORHOOD PRESERVATION OF STAMFORD
NEW BRITAIN HOUSING SITE DEVELOPMENT AGENCY

NEW BRITAIN MUSEUM OF AMERICAN ART
NEW BRITAIN, CITY OF
NEW BRITIAN HOUSING AUTHORITY
NEW CANAAN HOUSING AUTHORITY
NEW CANAAN LIBRARY
NEW CANAAN, TOWN OF
NEW ENGLAND ADOLESCENT TREATMENT CENTER
NEW FAIRFIELD, TOWN OF
NEW HARTFORD, TOWN OF
NEW HAVEN FREE PUBLIC LIBRARY
NEW HAVEN HOUSING AUTHORITY
NEW HAVEN, CITY OF
NEW LONDON HOUSING AUTHORITY
NEW LONDON LEDGE LIGHTHOUSE FOUNDATION
NEW LONDON MARITIME SOCIETY
NEW LONDON, CITY OF
NEW MILFORD, TOWN OF
NEWINGTON HOUSING AUTHORITY
NEWINGTON, TOWN OF
NEWTOWN, BOROUGH OF
NEWTOWN, TOWN OF
NOAH WEBSTER FOUNDATION
NOANK HISTORICAL SOCIETY
NORFOLK, TOWN OF
NORTH BRANFORD HOUSING AUTHORITY
NORTH BRANFORD, TOWN OF
NORTH CANAAN, TOWN OF
NORTH CENTRAL CT MENTAL HEALTH SYSTEM
NORTH HAVEN HOUSING AUTHORITY
NORTH HAVEN, TOWN OF
NORTH STONINGTON, TOWN OF
NORTHEASTERN CT REGIONAL RESOURCE RECOVERY AUTHORITY
NORWALK ECONOMIC OPPORTUNITY NOW INC
NORWALK HOUSING AUTHORITY
NORWALK HOUSING SITE DEVELOPMENT AGENCY
NORWALK REDEVELOPMENT AGENCY
NORWALK, TOWN OF
NORWICH HOUSING AUTHORITY
NORWICH, TOWN OF

OLD SAYBROOK, TOWN OF
OLD STATE HOUSE

PATHWAYS INC
PERCEPTIONS PROGRAM
PLAINFIELD HOUSING AUTHORITY
PLAINFIELD, TOWN OF
PLAINVILLE GROUP HOME
PLAINVILLE, TOWN OF
PLYMOUTH HOUSING AUTHORITY
PLYMOUTH, TOWN OF
PORTLAND HOUSING AUTHORITY
PORTLAND, TOWN OF
PRESTON HOUSING AUTHORITY

PROJECT LEARN INC
PROJECT MORE INC
PUTNAM HOUSING AUTHORITY
PUTNAM, TOWN OF

REGIONAL NETWORK OF PROGRAMS
REGIONAL SCHOOL DISTRICT # 01
REGIONAL SCHOOL DISTRICT # 05
REGIONAL SCHOOL DISTRICT # 06
REGIONAL SCHOOL DISTRICT # 07
REGIONAL SCHOOL DISTRICT # 09
REGIONAL SCHOOL DISTRICT # 11
REGIONAL SCHOOL DISTRICT # 12
REGIONAL SCHOOL DISTRICT # 13
REGIONAL SCHOOL DISTRICT # 14
REGIONAL SCHOOL DISTRICT # 15
REGIONAL SCHOOL DISTRICT # 16
REGIONAL SCHOOL DISTRICT # 17
REGIONAL SCHOOL DISTRICT # 18
REGIONAL SCHOOL DISTRICT # 19
RESCUE
RIDGEFIELD, TOWN OF
RIVERFRONT RECAPTURE INC
ROCKY HILL HOUSING AUTHORITY
ROCKY HILL, TOWN OF
ROSE CITY COMMUNITY LAND TRUST
RURAL HOMES

SALEM, TOWN OF
SALISBURY, TOWN OF
SCOTLAND, TOWN OF
SECOND CONGREGATIONAL CHURCH OF COVENTRY
SELF INC
SEYMOUR, TOWN OF
SHARON, TOWN OF
SHELTER FOR WOMEN INC
SHELTON HOUSING AUTHORITY
SHERMAN LIBRARY
SHERMAN, TOWN OF
SIMSBURY HOUSING AUTHORITY
SOCIETY FOR THE PRESERVATION OF NEW ENGLAND ANTIQUITIES
SOMERS HOUSING AUTHORITY
SOMERS, TOWN OF
SOUTH WINDSOR HOUSING AUTHORITY
SOUTH WINDSOR, TOWN OF
SOUTHINGTON, TOWN OF
SPRAGUE, TOWN OF
ST AGNES HOME
ST LUKE'S COMMUNITY SERVICES INC
ST VINCENT DE PAUL SOCIETY
STAFFORD HOUSING AUTHORITY
STAFFORD SPRINGS, TOWN OF
STAMFORD CENTER FOR THE ARTS
STAMFORD HOUSING AUTHORITY

STAMFORD, CITY OF
STERLING, TOWN OF
STONINGTON, BOROUGH OF
STONINGTON, TOWN OF
STRATFORD HOUSING AUTHORITY
STRATFORD HOUSING AUTHORITY
STRATFORD, CITY OF
SUFFIELD, TOWN OF
SUNSHINE PROJECT INC
SUSAN B ANTHONY PROJECT

TEAM INC
THAMES VALLEY COUNCIL FOR COMMUNITY ACTION
THERE'S NO PLACE LIKE HOME
THOMASTON, TOWN OF
THOMPSON, TOWN OF
TOLLAND HOUSING AUTHORITY
TOLLAND, TOWN OF
TORRINGTON HOUSING AUTHORITY
TORRINGTON YMCA
TORRINGTON, TOWN OF
TRUMBULL, TOWN OF

UNION, TOWN OF
UNITED COMMUNITY SERVICES INC
UNIVERSITY OF BRIDGEPORT

VALLEY RAILROAD CO., ESSEX
VERNON HOUSING AUTHORITY
VERNON, TOWN OF
VITNAM CENTER
VOLUNTOWN, TOWN OF

WADSWORTH ANTHENEUM
WALLINGFORD HOUSING AUTHORITY
WALLINGFORD, TOWN OF
WATERBURY DEVELOPMENT AGENCY
WATERBURY HOUSING AUTHORITY
WATERBURY, CITY OF
WATERFORD COUNTRY SCHOOL
WATERFORD PUBLIC LIBRARY
WATERTOWN HOUSING AUTHORITY
WATERTOWN, TOWN OF
WESLEYAN UNIVERSITY
WEST HARTFORD INTERFAITH COALTION
WEST HARTFORD, TOWN OF
WEST HAVEN COMMUNITY HOUSE ASSOCIATION INC
WEST HAVEN, CITY OF
WESTPORT HISTORICAL SOCIETY
WESTPORT, TOWN OF
WETHERSFIELD HOUSING AUTHORITY
WETHERSFIELD, TOWN OF
WHEELER CLINIC
WHEELER CLINIC

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WILLIMANTIC HOUSING AUTHORITY
WILLINGTON, TOWN OF
WILTON, TOWN OF
WINCHESTER HOUSING AUTHORITY
WINCHESTER, TOWN OF
WINDHAM TEXTILE & HISTORY MUSEUM
WINDHAM, TOWN OF
WINDSOR HOUSING AUTHORITY
WINDSOR LOCKS, TOWN OF
WINDSOR, TOWN OF
WOLCOTT, TOWN OF
WOMEN'S CENTER, THE
WOODBURY, TOWN OF
WOODSTOCK HOUSING AUTHORITY
WOODSTOCK, TOWN OF

YALE UNIVERSITY
YOUTH CONTINUUM OF TRI-RYC INC

BRIDGES, PIPES AND CONCRETE: CREATING THE WILL TO PAY FOR INFRASTRUCTURE

The problem, regardless of growth, is where to spend ever-limited resources. Some places are struggling successfully.

Cleveland's bridges, streets and water pipes were falling apart, along with its economy. With its population and that of its county in decline, the Rust Belt city faced the formidable task of finding the leadership and the funds to rebuild, repair and replace its corroding and outmoded infrastructure.

In fast-growing Raleigh, North Carolina, where the population in the city as well as its environs is growing explosively, the challenge has been to invest ahead of tomorrow's demand, to pay for the four-lane highways, expanded sewers and new water treatment plants that could keep pace with and maintain the city's growth.

Seattle and the four counties that make up the Puget Sound region sit on the horns of both dilemmas. The fast-growing counties and slowed-down city are saddled with the city's deteriorating infrastructure as well as the counties' demands for new roads and fire stations for a population that should grow by half a million more in the next decade. As in other older, urban environments, pressing social issues divert dollars away from infrastructure.

These tales of three cities, expanded in the three-part report that follows, underscore the difficult and varied political pressures local governments face in maintaining and investing in infrastructure, which is the basis for attracting or maintaining economic growth.

"Infrastructure isn't sexy. It isn't like a domed stadium or a microchip road peppered with computer companies," says Ohio Senator Michael White, a Democratic candidate for mayor in Cleveland. "You never miss your water until the well runs dry."

Infrastructure is also enormously expensive. Nationally, this year's need is expected to be double the $45 billion spent in 1985 for new and upgraded infrastructure, according to the National Council on Public Works Improvement.

On a local level, the figures are equally formidable. In the past decade, as Raleigh's population grew from 150,000 to nearly 200,000, voters in that city approved $165 million in bonds and the spending of nearly one-fourth of the combined capital and operating budget on infrastructure.

Creating the political will to make such investments—as well as failing to—is the subject the tales from three cities explore. The reports underscore observations Nancy Rutledge makes about cities that have successfully financed infrastructure. The executive director of the now-disbanded national public-works council says that three things are essential to creating citizen backing for infrastructure investment: an elected official who champions the cause, a business community that helps or leads the charge, and a capital planning process that systematically sets priorities for future investment.

Linda Birch illustration

DEVELOPMENT

RALEIGH: KEEPING UP WITH GROWTH

So far, there are no building moratoriums because of limited sewer capacity, and no citizen revolts because of gridlocked roads.

By Penelope Lemov

When Sarah Wilson moved to Raleigh, North Carolina, 20 years ago, she and her family struggled to find housing. IBM and other major corporations were opening offices in a new research and development complex called Research Triangle Park, about two miles from Raleigh. Newly transferred employees were gobbling up existing apartments and homes in the sleepy state capital. When the Wilsons finally found shelter, it was in the relatively undeveloped northern part of the city. The big house atop the hill on their street was a family estate; cows grazed in nearby pastures.

North Raleigh today is a sea of single-family houses, apartments, office buildings and shopping centers. The area is crisscrossed by four-lane highways that head north and east to further development, and south and west to downtown Raleigh, an international airport, the research park, and Durham and Chapel Hill, which also feed off and into the research park. The house on the hill is a restaurant, and the cows, notes Wilson, an assistant in the public-affairs office of Raleigh's city manager, are a memory.

Like other Sun Belt cities that have witnessed the arrival in their regions of high-tech research facilities, Raleigh is booming. The unemployment rate hovers around 3 percent. The total value of property has increased 15 percent a year over the past eight years. The population of the city, which is also home to North Carolina State University, has nearly doubled in 20 years, rising from 122,000 people in 1970 to an estimated 218,000 in 1988.

But unlike many fast-growing Sun Belt cities, Raleigh has managed, with minor fiscal bumps and political bruises, to pace the building of infrastructure to its growth. The future may be rougher going, but so far there have been no building moratoriums because of limited sewer capacity, and no citizen revolts because of gridlocked roads. Traffic is considered heavy when drivers wait at an intersection for more than one change of lights or have to slow below the speed limit on highways.

"We've tried to stay ahead of crises. People in this city want to have good-quality infrastructure, and they have invested heavily in it through budget and bond approvals," says City Manager Dempsey E. Benton Jr. Since 1980, Raleigh voters have authorized a total of $165 million worth of bonds to build local streets, roads in and out of the city (traditionally a state responsibility), parking facilities, parks, sewers, an addition to an auditorium and, most recently, a baseball stadium (as yet unbuilt).

Voters have gone along with budgets that apportion 24 percent of revenues for capital improvements. The property tax, following a revaluation of real estate in 1984, had been creeping up by about a penny every other year and increased this year by 6 cents to 72 cents per $100 of property valuation. Also, developers have begun to pay impact fees to cover a share (about 10 percent) of the cost of roads and open space in areas in which they build.

Two things have made such financing possible. One is the nature of the population that's been arriving in Raleigh for the past 20 years: well-educated, white-collar professionals, many from cities where the infrastructure has deteriorated. "They let us know that they didn't want that to happen in Raleigh," Benton says. "They encouraged us to invest money in infrastructure."

The other reason is a political process that keeps voters informed about and involved with infrastructure issues. The process, first used in 1979, starts with a five-year capital improvements plan that inventories existing infrastructure and identifies projects for improvement or expansion. "It is a working document that guides the city administration in scheduling and constructing facilities in Raleigh," says Benton. It is also a document that is debated by the city council during both pre-budget and budget hearings. Projects that will be funded by the budget, and bigger projects that will be funded by bonds, are duly noted and discussed. They are also presented for discussion and comment to the city's 18 citizen-advisory committees.

"It's a never-ending process. There are occasions when we say we should have worked harder in informing people, but we have a commitment to an open process. It's the people's business we're about. We don't cut deals in back rooms," says Mayor Avery Upchurch.

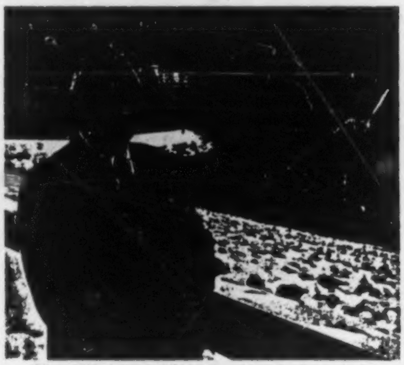
Major infrastructure projects are designed to be citywide. Each time park or transportation projects are planned, each part of the city gets a share of the improvements. "That, to me, has been one of the elements built into our success," says Upchurch.

Once a project is approved, Benton's office moves quickly to start construction within 18 months. "We have a strong emphasis on a short turnaround time between appropriation and availability of services," Benton says. "We want to have credibility when we go back to our voters for the next project."

Priorities for funding projects are set by the city council. For the most part, infrastructure is Raleigh's responsibility; social welfare and education are Wake County's. Officials in both governments coordinate their efforts to tap public willingness to finance major programs. "Raleigh represents 55 percent of Wake County voters, so we don't want to go to voters at the same time for approval of competing issues," Benton says. Accordingly, the city went to its voters in 1987 with a $97.5 million bond referendum for roads, parks and utilities; the county clocked in last year with a $125 million referendum on education. Both passed with more than 70 percent of the vote.

The city apportions $2.2 million of its $164-million-a-year capital and operating budget to such social programs as Meals on Wheels and assistance for the homeless. With a healthy and growing economy, however, Raleigh's social problems are not on a par with those of such large cities as New York. They have not, in short, had an impact on the city's ability to fund infrastructure during the 1980s.

That could change in the coming decade, not because the economy will falter or social problems increase, but because the city faces growing restrictions on its ability to raise revenue. The state legislature has rescinded the authority of local governments to tax personal property. The state funds apportioned to the city of Raleigh to cover that revenue loss, says Benton, do not accommodate the city's rate of growth, which direct taxation would have covered. In addition, the state mandated an increase in retirement benefits for law enforcement officers. "In the past, such mandates were accompanied by revenue to cover the mandate. They didn't do that this time," Upchurch says.



The public is kept informed and 'we don't cut deals in back rooms,' says Mayor Avery Upchurch.

One way the city is attempting to make up for the decrease in revenue is through increased user fees on such items as automobile ownership decals and by imposing impact fees on developers. These impact fees, which went into effect after three years of negotiation, are assessed on developers and builders based on the size and type of project they are constructing.

Although the development community has, so far, been fairly sanguine about them, the fees represent a potential fiscal shoal for the city. Not one of Raleigh's neighbors in the Research Triangle area imposes such fees. There is concern that developers could move out of Raleigh to other nearby cities, where it is less expensive to build. "We depend on our tax base to fund government obligation bonds. We need development to maintain our growth," says Benton of the city's sensitivity to the fees.

Smedes York, mayor of Raleigh from 1978 to 1983 and president of York Construction Co., notes that the development community does not "embrace the fees, but there hasn't been a mass exodus. The reason Raleigh could put the fees in is that there was a strong market here. There's some overbuilding now, and that could make the fees less palatable."

Historically, Raleigh's development community has cooperated with the city to help finance infrastructure. In 1985, for instance, developers agreed to pay sewer hookup fees in advance, thus financing one-third of the $9.1 million cost of building 17 miles worth of new sewer lines and a pumping station. This relatively quick fix helped work out a compromise on another sewer problem. Private developers had begun constructing their own small sewer plants to serve developments built beyond Raleigh's sewer service area. With the financing in hand to expand the sewer system, city officials were able to work out arrangements with the developers to abandon their private plants and connect to city sewer lines once those lines are constructed.

If there's one criticism developers like York have about Raleigh's infrastructure program, it is that the city has gotten bogged down in regulation in the past few years, and so has failed to move ahead quickly with such projects as the minor-league baseball stadium. "They also let an arena get away from them," says York. "The city council needs to move out in front on progressive issues."

Raleigh's capital improvement future is also clouded by the growing need for regional solutions to many infrastructure problems, such as solid-waste disposal and watershed protection. The region ranks in the top 20 for its state-of-the-art regional planning, claims Chapel Hill Mayor Jonathan Howes, who was president of the National Association of Regional Councils. On the other hand, he adds, "like most parts of the country, regional implementation is primitive. We in local government are reluctant to grant power or decision making to supralocal bodies."

Meanwhile, Raleigh's mayor plays an active role on committees and projects that are part of regional council-of-governments efforts. He also is actively lobbying state and federal governments for infrastructure assistance. And he and the city council are looking at ways to adjust the budget. "We may have to cut back, but fortunately, many of the improvements we made during the 1980s will carry us into the next decade." ☐

Kerra Tom photograph

DEVELOPMENT

CLEVELAND: COMING OFF THE BOTTOM

County and city both are still declining, but a savvy coalition is finding the money for rebuilding. Can it keep ahead of the decay?

By Cynthia Kyle

Water pipes in Cleveland, laid before 1955, were corroded and clogged to the point that service to hundreds of customers was being cut off at peak demand hours. The condition of the pipes threatened the city's response to fires, and a county judge declared the system a danger to human health and safety. So severe were sewer maintenance cutbacks that the city could respond only to emergencies: street cave-ins or reports of sewage flooding into basements. A third of the bridges in the city's care needed major work; so did a like number of streets. Even the roof of Cleveland's handsome granite city hall leaked.

Years of neglect, refusal to raise taxes and political bickering had taken their toll on the Lake Erie city once touted as the "best location in the nation" but since derided as "the mistake on the lake." Unemployment was up and the population, in surrounding Cuyahoga County as well as in the city, was shrinking dramatically.

Cleveland's financial bookkeeping was declared unauditable. Locked out of the capital markets by its default in 1978—the first default of a major U.S. city since the Depression—Cleveland could barely come up with its share of the money to match federal and state funds available for infrastructure overhaul.

Finally, in 1979, the city endorsed an income tax increase; elected George V. Voinovich, a Republican and former lieutenant governor, as mayor; and set out to reclaim itself. Riding a business-backed campaign into city hall, Voinovich called himself the "private-public partnership mayor."

Indeed, the day after his election, executives from eight major accounting firms and four major corporations agreed to a pro bono financial audit of the city. The verdict, after 11 weeks of work: $110 million in accumulated budget deficits that had to be paid off somehow.

In the next two years, 90 loaned executives would recommend 650 ways for the city to operate more efficiently, and Cleveland voters would approve yet another income tax increase. Half of the new tax, set at 2 percent, would retire the city's debt. The other half would finance infrastructure repair. A systematic process for setting priorities—a five-year capital improvement plan, updated every year—was put in place. Wall Street responded by boosting the city's credit rating in the summer of 1981, and the stage was set to rebuild.

Repair or replacement of fire stations, some dating back as far as 1875, came first, because of their impact on life and safety. But fixing the leaky roofs of recreation center buildings got high priority, too, because the public wanted their indoor swimming pools and other facilities; it was a way of building public support for the infrastructure repair effort. All totaled, the first five-year plan, covering the 1981-1986 period, identified $400 million in deferred maintenance needs. City hall's roof was fixed in 1985.

Reconstruction is now under way on the city's ancient Division Avenue water plant, built in 1915 and formally designated as in "hazardous condition." The price tag: $102 million.

In another three years, the city expects to rehab or replace 17 Cuyahoga River bridges that connect major industrial routes. The city is starting replacement of another 17 bridges, mostly arterial railroad crossings constructed in the 1920s.

"We're trying to catch up," says Richard Halishak, commissioner of engineering and construction. "Sometimes we close more than we open." As of March, four bridges remained closed because of their condition and five more bridges were closed for construction.

The latest five-year plan includes neighborhood development projects for the first time: demolition of vacant and vandalized buildings that can't be saved and renovation and code enforcement of those that can, in both residential and commercial districts. The overall price tag for the five years: $1.01 billion. Some $740 million of it will come from local sources, the rest from federal programs and the state. That the city had to hit bottom before it could pull itself up by the bootstraps "is an unfortunate statement of fact," says Finance Director Charles Brown.

George Peterson, a researcher at the Urban Institute, which in 1979 found Cleveland's infrastructure among the nation's worst, is impressed by the city's transformation. "What's unique about Cleveland is the human network that's been able to keep infrastructure at the top of its priorities," he says.

The hub of the network, an organization known as Build Up Greater Cleveland, was formed in 1983 by the Greater Cleveland Growth Association, a regional chamber of commerce with 8,500 member companies in seven northeastern Ohio counties. Major financing came from Cleveland-based charitable foundations.

What is notable about Build Up, as explained by its director, Walter Olson, a retired National Aeronautics and Space Administration executive, is the way its members

Cynthia Kyle is a Michigan-based free-lance writer.

were selected. "We picked positions, then we asked the people to serve. No matter who the people were, we needed the position."

Among those named to Build Up's policy committee through this bald but savvy strategy: the president of the Cuyahoga county commission, a Democrat; the president of the Cleveland city council, a Democrat; the Cuyahoga county engineer, who has authority over all suburban road and bridge-repaving projects; Mayor Voinovich and key financial and public-works members of his cabinet; a bank officer who handled government bond projects; the vice president of a major oil company, one of the city's leading employers; and U.S. Representative Louis Stokes, a Democrat with 20 years of service in Congress and a key seat on the House Appropriations Committee.

Stokes believes that Cleveland found the political will to deal with its problems because of "the growing maturity of the business community in terms of their relationship with the political infrastructure of the city.... Whether we're Republicans or Democrats, it's our city."

"United we stand and make progress," says Voinovich. "Divided we weren't getting very far."

Through its collective lobbying efforts, Build Up has nailed down such revenue sources as $122.4 million in federal funds for roads and bridges, $81 million in federal funds for transit, $22.6 million in federal wastewater construction grants and $40 million in federal transportation funds as the city's share of a state allocation. "We looked everywhere we could for money," says Olson. "We'd go to a committee in Washington and say 'Here's our plan and here's the expected federal role. Who expects it? We expect it.'"

The city had to hit bottom before it could pull itself up, says Finance Director Charles Brown.

"It also didn't hurt to have a Republican at city hall and a Republican in the White House," says Norman Krumholz, professor of urban planning at Cleveland State University and former director of Cleveland's planning commission.

Lobbying in Columbus and around the state, with some 40 polished speakers, Build Up helped persuade Ohio voters to approve a $1.2 billion bond issue in 1987 to finance infrastructure work. The proceeds of the issue promise $14.5 million annually for the next 10 years for Cuyahoga County improvements.

Cleveland helped itself by raising water rates and income taxes—though efforts in 1984 for a third income tax increase failed—and by repeated forays into the bond market, once its credit was re-established. It sold $153.3 million in waterworks improvement bonds in 1987, the largest offering in the city's history. Both the city and Cuyahoga County took advantage of state legislation authorizing increases in local motor vehicle license fees.

To be sure, there is some grumbling. Dennis Kucinich, the Democrat who was mayor during the city's default, complains that political leaders and private businesses are too cozy. "The private-public partnership is two hands in the taxpayers' pockets instead of one. In Cleveland, business is the government."

Other Democrats cheer. "If we don't make repairs, if we don't replace the old, [corporate chiefs] will say goodbye, and with them will go thousands of jobs," says Senator Michael White, a Democratic candidate for mayor. During 1988, the Greater Cleveland Growth Association recorded new corporate investment of $98 million and nearly 1,500 new jobs. "Without new roads and bridges, people would turn elsewhere to establish their businesses," says another mayoral hopeful, Cuyahoga County Commissioner Timothy Hagan. "You can sell that position without selling your soul." He thinks the private-public partnership and its accompanying tax increases were more politically palatable because the taxes were levied for specific rather than general purposes and their need was undebatable.

Now, uncertainty confronts the city. Voinovich, the city's longest-serving mayor, who lost his 1988 bid for U.S. Senate, must decide before summer's end whether he will seek re-election. The flow of new federal money is, at best, problematic, whatever the city's clout in Washington. The Environmental Protection Agency is threatening to impose an estimated $20 million in sanctions unless the legislature empowers Cleveland to start an automotive emissions testing plan to curb carbon monoxide pollution. Penalties could include a ban on industrial construction and the loss of federal sewer funds.

Economic experts warn of recession, although Voinovich thinks the city's more diversified economy means that "our back will not be broken like it was in the '80s." The city's population is still declining; a Cleveland State University researcher projects a further decrease of some 100,000 by 2005, from the 1986 Census Bureau estimate of 536,000. The suburban count could continue to drop, too, something that is not happening in most other old Rust Belt areas.

"You can ask: If we've been so good at raising money, why hasn't the problem gone away?" Olson says. "That simply reflects the fact that... the infrastructure is eroding as fast as you fix it." ☐

Barney Taxel photograph

DEVELOPMENT

SEATTLE: DEFEATED BY THE SPRAWL

A booming population, spreading outward with ever-decreasing density, tests the will and the resources to provide basic needs.

By John Herbers

The Puget Sound region in and around Seattle has long provided one of the most livable urban and rural environments in America. In recent years, it has become a vibrant economic unit as well, covering 6,294 square miles of scenic land in four counties that are home to 2.6 million people—a kind of paradise on earth, many of them will tell you, with fingers of land stretching into blue waters, the grade of the hills providing the maximum view of the emerald landscape, and everywhere tapered evergreens bathed by mist. On a clear day, the snow-covered peak of Mount Rainier rises majestically on the horizon.

But wait. There is trouble in paradise. Another half a million people are expected by the year 2000, and residents already are finding they can no longer get to work or to the lakes and mountains in 20 minutes, or even an hour. Bookstores are doing a booming business among those who want more than newspapers to read in traffic jams. Powerful no-growth movements are under way among citizens in rural and urban areas alike.

Government, business and civic leaders are furiously looking for ways to control the growth without wiping it out and to build and maintain the streets, roads, bridges, ferries, public buildings, and water and sewer systems needed right now. One statistic will serve to exemplify the growing needs and the lack of adequate response. The miles traveled on highways in King County, the region's most congested, more than doubled from 1965 to 1985, from 18 million to 42 million, yet the amount spent for capital improvements has declined (in dollars of constant value) from $390 million to $300 million, and for maintenance from $450 million to $350 million. Tax revenues were diverted to more politically popular programs, education among them. The gap between miles traveled and money spent continues to widen.

In the Puget Sound region, the difficulty is not the lack of resources or of a political culture that supports governmental action. Indeed, William Stafford, director of intergovernmental relations for Seattle, points out that the vote in the Puget Sound region carried the state for Democratic presidential candidate Michael Dukakis. Proposals calling for ambitious new tax levies to wipe out the infrastructure deficit come from various leadership groups, including the business community.

The trouble lies with the fractured system of government, which has had its weaknesses magnified by the decline in aid from the federal government. In addition to the four county governments, the region encompasses 71 municipalities, more than 1,000 special-service districts and three Indian reservations, all with taxing authority and all in the business of delivering services.

Only the state government is in a position to step in and impose regionwide solutions, but the state has been more hindrance than help. Washington's government resembles those of most Southern states of two decades ago, with a constitutionally weak governor's office and a strong legislature dominated by rural interests. The legislature is particularly restrictive about what taxes local governments may raise and how the money is spent. The urban areas of western Washington, which pay one-third of the gasoline taxes that go into the state's treasury, get only about 6 percent back.

As the pressure has mounted on officials in the Puget Sound region, they have become quarrelsome and further divided on approaches to solving their problems. Seattle's Democratic mayor, Charles Royer, who in the past 11 years has presided over a downtown building boom and construction of thousands of housing units for poor and moderate-income residents, has wearily announced that he will not run for re-election when his term ends later this year. He has watched Seattle lose its supremacy, and much of its political clout, both in the legislature and within the region, as the population around it has burgeoned while the city has struggled to stem its decline.

Royer says the governmental structure in the Puget Sound area is like the state's complex, inequitable tax structure: "Each is a patchwork so out of date and out of balance that it cannot meet the demands of our region."

Life isn't paradise either for Tim Hill, the elected executive of King County, who has the same powers as a strong mayor. As head of the largest unit of government in the region, Hill would be expected to take the lead in achieving a regional approach in building and maintaining infrastructure. But he is constantly on the defensive and under attack from the county's 29 municipalities and his own council members.

Under state law, county taxing authority is very limited. Counties cannot levy business and occupation taxes or utility taxes, as municipalities are permitted to do. Instead, King County keeps raising the sales tax to its allowable limits, now above 8 percent, while the municipalities attack it for spending money collected within their borders to provide urban services to residents of unincorporated areas.

The situation is further complicated by a proliferation of special-service districts.

Aside from the state, the only overarching agency that could make sense out of this crazy quilt of governments is the Puget Sound Council of Governments, but it has no power except that voluntarily delegated to it by its component governments. Its only significant power now is planning an areawide transportation system. Yet the King County council, over Hill's objections, recently withdrew most of its financial support for the organization because, according to County Council Chairman Gary Grant, it was not getting anything done "on the tough issues of forging regional mandates." Hill, a moderate Republican, thinks that the action only hurt efforts for regional agreement.

If that were not enough, residents of unincorporated urban areas have been clamoring to be annexed to towns and cities because the county is unable to pay for all the urban services they want, including police protection. Hill would like to see that happen, because the county could then focus on providing traditional county services such as health care and jails. But members of the county council are opposed because they would lose many of their constituents.

Tim Hill, King County's elected executive, tries for a regional approach but rarely succeeds.

Against this backdrop, there are symbols that show the need and the seeming inability of government to meet it.

In Seattle, there is a narrow, ancient bridge on First Avenue that has been in need of replacement as long as most people can remember. It has been the cause of huge traffic jams and several deaths. It is owned and operated by the state as part of its highway system, but neither state nor local officials have ever found the funds, now estimated at about $100 million, to replace it. Nor can the city put its hands on enough money to properly maintain its streets, according to Ken Bounds, assistant city budget director for infrastructure.

A few miles north of Seattle, in Snohomish County, there is a new 1,078-acre, Japanese-planned community called Mill Creek. The development has brought severe traffic tie-ups on nearby highways. At least 10 development companies are planning similarly large housing communities in rural areas stretching from Snohomish County to south of Tacoma.

In the northern part of King County, there was a heated controversy over plans for 7,500 new homes and 2,500 apartments. The county, following a master plan of two years ago that called for higher densities, wanted to zone the land at one housing unit per acre. The compromise ultimately reached, balancing the demands of builders, slow-growth rural residents and environmentalists, permitted the development but zoned the land beyond it at one house every five acres.

Meanwhile, back in Seattle and other urban areas, citizens have gotten up ballot initiatives which, if approved, would slow development by putting a cap on construction. This, according to Royer and others, would only force more growth into the outlying, low-density part of the region, whose infrastructure needs are not being met now.

Still, there is so much energy, innovation and public interest throughout the region that a workable plan for infrastructure could well emerge as a matter of pure necessity. The various governments have taken a partially regional approach to sewage treatment and disposal through an agency called Metro. Tunnels are being built under downtown Seattle for buses and ultimately light trains. Multiple plans are on the boards for solving the infrastructure crisis, although there is no overall master plan the interests can agree to.

For now, the only relief in sight seems to be another, almost certain increase by the state in the gasoline tax and a change in the distribution formula. Bills that would add anywhere from 3 to 9 cents per gallon to the present 18-cent levy are under debate in Olympia. But whatever the increase, it will be far from all that is needed.

What the citizens and officials of the Puget Sound region have not focused on is the real nature of their infrastructure problem. It goes beyond simply finding the political will to raise taxes or even the more difficult task of modernizing obsolete governmental structures. The underlying question is whether government can, in fact, be expected to maintain and repair the old infrastructure in aging, dense cities and simultaneously build the new facilities in communities of very low density that are expanding almost without restraint.

The number of persons per housing unit shrinks every year, with fewer people getting or staying married, more single-parent homes and fewer children. The density of housing units per square mile also shrinks, as development reaches into the countryside. The greater the distance between households and the smaller the households, the more bridges, the more miles of asphalt and concrete, pipes and wire that will be needed. This is the fundamental problem that countless areas across the nation, along with the Puget Sound region, have not yet confronted. ☐

Matthew McVay/Picture Group photograph

ESSAYS ON ISSUES

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Rx for productivity: Build infrastructure

A six-car collision on Tampa's two-lane Howard Frankland Bridge—the locals call it the "Frankenstein"—causes a three-hour traffic jam during rush hour. A dam bursts near Toccoa, Georgia, killing thirty-nine residents—mostly children—of a tiny Bible college. A bridge collapses on Interstate 95 in Connecticut, hurling six people into the river some 75 feet below, killing three and injuring several others.

Such accidents and disasters happen almost daily in the United States. They are outward signs of a growing affliction—the decay of our national infrastructure. But not only safety and convenience are affected. There are deeper implications of this national neglect for the health of the U.S. economy. Indeed, as Bill Clinton, Governor of Arkansas, recently wrote, "America is falling apart, literally. Federal budget pressures and changes in the Federal tax law in the 1980s have steepened a decline in public works spending that dates to the 1950s."[1]

This *Letter* looks at recent trends in public works expenditures and relates the fall-off in such spending with the productivity slowdown that became evident in the United States around 1970. The decline in public capital spending—on dams, highways, sewers, mass transit, etc.—relative to employment and private investment in plant and machinery forces private business to absorb higher costs, and thereby lowers productivity. And lower productivity, sooner or later, means a lower standard of living.

A stronger commitment to America's infrastructure by the public sector is necessary for at least two reasons. First, a well-maintained public works system contributes to an expanding, robust economy. Second, directly and indirectly, it contributes to an improved standard of living.

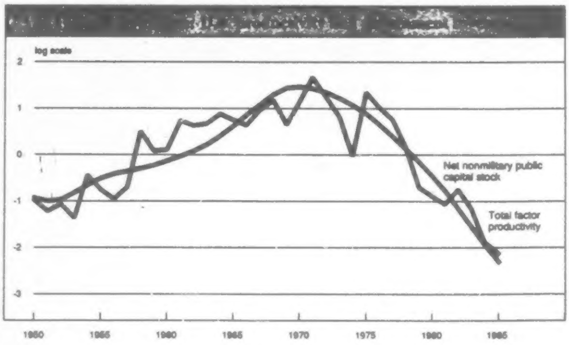
A check-up

On the basis of most external appearances, the economy's health is robust. We are experiencing an expansion of output that is progressing into its sixth year; economists are raising their forecasts for this year's growth rate of gross national product (GNP); we see surging employment and a declining unemployment rate. To be sure, we see some threats of inflation, but not the inflation fever of other periods.

A complete physical examination, however, produces evidence of economic atrophy. The growth of output that is not explained by increases in labor and private capital inputs—generally called "total factor productivity"—has slumped during the last decade and a half. Indeed, the annual growth rate of total factor productivity in the private business economy has plummeted from 1.5% from 1951 to 1960 and 1.8% from 1961 to 1970 to 0.8% in the 1970s and a dismal 0.7% in the first half of the 1980s.

When an economy begins to produce less per worker, as has been the experience in the United States of late, commonsense suggests various possible solutions. Households can scale back consumption purchases in line with reduced income growth. Firms can reduce expenditures on capital goods in the face of lower profit margins. Or the government can reduce its own spending on goods and services (consumption spending), leaving a larger slice of output to be allocated to competing private sector needs. However, none of these resolutions have occurred, or at least have not occurred sufficiently enough to match the diminished availability of domestically produced goods and services.

Instead, households, businesses, and the government have saved less and borrowed more in the attempt to consume, invest, and finance public spending in excess of their income, cash flow, and tax revenue.



After averaging 9% of GNP during the 1960s, the private savings rate fell to 8.3% during the 1970s and even lower, to 6.2%, during the first half of the 1980s. Also, there has been a high budget deficit as the government sector's outlays exceeded the pace set by tax revenues. During the last years of the Carter Administration and throughout the Reagan Administration, budget deficits ballooned, with the excess of spending over revenues peaking at 5.4% of GNP in 1984.

In turn, the national attempt to spend beyond our present means has forced up real interest rates as well as caused a trade deficit in the international accounts. Higher interest rates work to choke off private expenditure, particularly on durable goods, thereby lowering the demand for borrowed funds. At the same time, higher domestic interest rates—relative to foreign rates—also attracted foreign capital. This had the desirable effect of allowing a higher private investment rate, thereby enhancing future productive capacity, than would have occurred in an economy closed off from international capital markets. Still, this has resulted in a large liability to the rest of the world. Indeed, by most accounts, the United States went from being the world's largest creditor to the world's largest debtor in less than a decade.

The ultimate consequence of the productivity disease then will be a lower standard of living as we pay back the debt held by foreigners.

Previous diagnoses

Prior studies of the fall-off in productivity have centered on a relatively small number of potential causes. A surge in aggregate productivity can be expected whenever resources are shifted from less to more productive sectors of the economy. The migration of labor from farm to nonfarm occupations had such an effect, but mostly came to a halt by the mid 1960s. Certain economists, most notably Zvi Griliches of Harvard University, have emphasized a general slowing of expenditures on research and development and a related slowing of technological change.

of:	1950-85	1950-70	1971-85
Productivity	1.5%	2.0%	0.8%
Public capital	3.0%	4.1%	1.6%
Public capital relative to private inputs	1.1%	2.4%	-0.6%
Capacity utilization	0.2%	0.3%	0.1%

But, the combination of these factors does not go far enough in explaining the productivity decline. The Bureau of Labor Statistics, for example, estimates that these factors probably account for only one-fourth or so of the slower productivity growth in the private economy. Lower rates of capacity utilization also may explain some of the reduction in total factor productivity; after averaging 84.1% during 1951 to 1970, the rate of capacity utilization fell to 79.5% in the period 1971 to 1985. But changes in capacity utilization rates, largely driven by erratic fluctuations in aggregate demand for goods and services and transitory technological shocks, are more likely to explain short-term, rather than long-term movements in productivity.

A new diagnosis

One place to search for a plausible reason for the productivity decline is in the government accounts—how the government gets and spends its money. Many have insisted that the financial status of the public sector—the budget deficit and consequent creation of government bonds—may play an important role in influencing the economy's performance. Specifically, it is argued that high public sector bond issuance forces up real interest rates and drives down the new private investment spending that is essential for fostering economic growth and technological improvement.

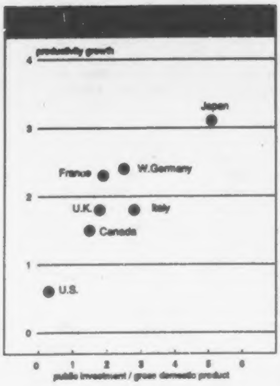
I suggest, however, that it is more reasonable to look at the physical aspects of the government budget, at the distribution of government spending across various broad categories.

As it happens, there is a remarkable correlation between the level of total factor productivity and the level of the nonmilitary public capital stock over the last thirty-five years. My empirical results suggest that movements in public capital are capable of explaining a large portion of the longer term movements in productivity in the private sector over the period 1949 to 1985.[2]

Roughly, a one percentage point increase in the level of the net stock of public capital relative to the level of private sector inputs of labor and capital brings forth a one-third of one percentage point (.33) rise in productivity. Table 1 translates this result into an accounting mechanism for the growth rate of total factor productivity during the high-growth period 1950-70 and the subsequent low-growth period 1971-85. While productivity growth fell from 2% to 0.8% per year—a fall-off of 1.2 percentage points—the growth rate of the net stock of nonmilitary public capital shriveled from 4.1% to a mere 1.6% per annum. Even more strikingly, the growth rate of the public capital stock *relative to* a "combined" unit of private labor and capital went from a strongly positive 2.4% to a *negative* 0.6% in the slowdown period.

Multiplying the slump in the growth in public capital by the sensitivity of productivity to public capital growth—the previously mentioned 0.33—shows that fully (3.0) x (.33) = 1.0 percentage point of the total decline in productivity of 1.2 percentage points can be attributed to the neglect of infrastructure.

Figure 1 vividly illustrates the tight relationship between public nonmilitary capital and total factor productivity by comparing levels of total factor productivity and the stock of public structures and equipment after removing time trends. As is clearly demonstrated, this relationship holds for the period of rising productivity growth during the 1950s and 1960s as well as for that of falling productivity growth during the last decade and a half. And, as low productivity growth leads a low standard of living by the hand, insufficient investment in the economy's infrastructure will soon force individuals to trim their style of living; Senator Quentin Burdick of North Dakota warns, "We have produced a high standard of living, but we are beginning to see cracks in that high stand-



ard, and a less than adequate infrastructure has been identified as the cause."[3]

We would also expect that countries that sustain a high level of public investment relative to output would experience higher productivity growth than countries that do not invest in infrastructure. Figure 2 illustrates precisely this result, plotting combinations of annual growth rates of gross domestic output per employee hour and ratios of public investment spending to gross domestic output for the "G-7" countries over the period 1973-85. Japan has invested about 5.1% of output in public facilities and achieved productivity growth of 3.3%; at the other end of the spectrum we find the United States with a low public investment of 0.3% per year and low productivity growth of 0.6% per annum. At the same time, productivity growth in these countries was negatively related to government consumption spending.

While total government outlays relative to GNP have risen from 26% in the late 1950s to 35% in the middle of the 1980s, public nonmilitary capital expenditures have slid precipitously. Dana Huestis, President of Associated General Contractors of America, has stated in Congressional testimony, that "the infrastructure crisis is real. As a nation, we have not been investing enough in our public facilities to either keep up with new growth, or to rebuild and protect what is falling into disrepair."[4]

Thus, a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, port facilities, airports, and other facilities which aid in the production and distribution of goods and services. Just as thoughtful athletes would not think of neglecting their health for fear of failing to compete well on the playing field, we as a country should be vitally concerned with the viability of our economic lifelines that enable us to meet the challenge of an increasingly competitive world marketplace.

In the words of Nancy Rutledge, Executive Director of the National Council on Public Works Improvement, "If we spend too little on public works...society loses more than the direct public cost. In the long run, our ability to compete in the international economy will be weakened, and our standard of living will suffer."[5] Nearly echoing her remarks, Peter Butkus, a public works manager for the State of Washington, has said that "good public works becomes the single most important thing that local governments can provide in the nation's effort to maintain and expand foreign trade and competitiveness."[6]

Prognosis

The chance for a recovery from a physical condition such as a minor hardening of human arteries is usually quite good if it is identified early enough, and the patient adopts a proper counting of calories, a good diet, and a certain amount of exercise. Similarly, given the stability of the relationship between the economy's infrastructure and the productivity of private factors of production, we may be confident that a more balanced distribution of public sector resources, shifting some from consumption and into capital accumulation, will rejuvenate the economy's lifelines. **Raising the level of public investment spending from its current abysmal level of less than one half a percent of GNP to a modest two percent—some 80 to 90 billion dollars per year—would work wonders, quite likely wonders comparable to those of modern medicine in dealing with human disease.**

— David Alan Aschauer

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[1] "America is Buckling and Leaking," *New York Times*, June 24, 1988.

[2] These estimates are contained in David Alan Aschauer, "Is Public Expenditure Productive?" Federal Reserve Bank of Chicago, working paper, in press.

[3] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, October 21, 1987.

[4] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, October 6, 1987.

[5] *Fragile Foundations*, National Council on Public Works Improvement, February 1988.

[6] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, November 4, 1987.

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Fragile Foundations:
A Report on America's Public Works

Final Report to
the President and the Congress

National Council on Public Works Improvement

February 1988

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Senior Managing Director of Public Finance for the investment banking firm of Bear, Stearns & Co., Inc. Born in Bayonne, New Jersey, he previously served as a cabinet officer under Governor Hugh Carey of the State of New York (1977). He was Chairman of the U.S. Senate Budget Committee's Private Sector Advisory Panel on Infrastructure Financing (1985–1987). He is a graduate of Rutgers University (1967), and holds master's degrees in public administration from New York University (1972) and in business from Columbia University (1977). Mr. Giglio was appointed to the Council by the President pro tempore of the U.S. Senate.

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Former Executive Director of the Port Authority of New York and New Jersey (1977–1985), currently Group Vice President, Eastern Newspapers for the Times Mirror Company. Born in New York City, he served as Director of the Budget for the State of New York (1975–1977) and Secretary of Human Services for the Commonwealth of Massachusetts (1971–1975). He is a graduate of Harvard College (1962). Mr. Goldmark was appointed to the Council by the Speaker of the U.S. House of Representatives.

Freeman Holmer

Former Vice Chancellor for Administration of the Oregon State System of Higher Education (1969–1979), currently President of the City Council of Eugene, Oregon. Born in St. Paul, Minnesota, he previously served as Director of Environmental Protection for the State of Wisconsin (1966–1968) and Director of Finance and Administration for the State of Oregon (1959–1966). He is a graduate of Concordia College (1938) and holds a master's degree from the University of Oregon (1946). He was professor of political science at Willamette University (1949–1959) and at New York University (1946–1949). Mr. Holmer was appointed to the Council by President Reagan.

Lowell B. Jackson

Registered Professional Engineer, currently a private consultant in Aurora, Colorado. Born in Milwaukee, he served this past year as Chairman of the Executive Committee of the Transportation Research Board. He was Secretary of Transportation in the State of Wisconsin (1979–1981, 1983–1986) where he also served as Secretary of Labor (1981–1982), and was Director of the Colorado Department of Highways (1987). His civil engineering degrees are from Purdue University (1957, 1959), where he was a member of the faculty (1957–1965). He also was a tenured faculty member at the University of Wisconsin (1965–1978). Mr. Jackson was appointed to the Council by President Reagan.

Frieda K. Wallison

Partner in the law firm of Jones, Day, Reavis & Pogue. Born in New York City, she previously served as Executive Director and General Counsel of the Municipal Securities Rulemaking Board (1975–1978). She also was Special Counsel of the Securities and Exchange Commission (1975). She was a member of the National Council on Governmental Accounting, and now serves on the Governmental Accounting Standards Advisory Council. She is a graduate of Smith College (1963) and holds an LL.B. from Harvard University (1966). Mrs. Wallison was appointed to the Council by President Reagan.

Nancy S. Rutledge, Executive Director

Former Director of the Washington State Public Works Project (1982–1985). Prior to joining the Council, she was an investment banker with the firm of Seattle-Northwest Securities, Inc. (1985). Born in Olympia, Washington, she is a graduate of Pacific Lutheran University (1970) and holds a master's degree in public administration from the John F. Kennedy School of Government at Harvard University (1979).

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Preface

The National Council on Public Works Improvement (the "Council") was created by the Public Works Improvement Act of 1984 (P.L. 98-501) to assess the state of America's infrastructure. The results of that evaluation are presented in a three-part document, ***Fragile Foundations: A Report on America's Public Works.***

- Part One summarizes the Council's findings and its conclusions about the capacity of the nation's infrastructure to support future economic growth. It also outlines the Council's proposed strategy for strengthening these facilities and restoring a clear commitment to the future.
- Part Two provides a synthesis of major themes from over 5000 pages of research material prepared for the Council during the past two years. All of the research findings were reviewed and commented on by a wide range of public works experts in dozens of working group meetings, public hearings, and other public forums.
- Part Three is an Appendix that analyzes the performance of eight major categories of public works.

The three parts of this report represent the Council's final submission to the President and the Congress. This document is Part One of that report.

The Council's first report, *The Nation's Public Works: Defining the Issues*, provided an overview of current knowledge and set a broad context for further discussion and research. The issues included public works needs, economics and finance, government roles, management and decision making, and technological innovation. That report was submitted to the President and the Congress in September 1986.

The second report took the form of a series of study papers commissioned by the Council from independent consultants on nine categories of public works facilities and services: highways, streets, roads, and bridges; airports and airways; mass transit; intermodal transportation; water resources; water supply; wastewater management; solid waste; and hazardous waste. Each paper addressed the main issues identified by the Council in its first report. In the final chapter of each paper, the consultants provided the Council with their own views on major policy options in that category. These recommendations were reviewed by the Council but have not necessarily been incorporated into the Council's final policy conclusions. The entire series was transmitted to the President and the Congress in May 1987.

The Council also commissioned several analyses of cross-cutting themes that emerged from earlier work. These included: the role of dedicated revenues and special districts in funding public works; the unique problems of small public works systems; the link between infrastructure and economic activity; how other nations view infrastructure in their economic development efforts; the adequacy of the nation's public works; and improving the performance of public works through better management and decision making.

The Council has found much that is good about what cities, counties, special districts, states, and the nation are doing in planning, building, operating, and maintaining America's infrastructure. But on balance, the Council concludes that our infrastructure is inadequate to sustain a stable and growing economy. As a nation, we need to renew our commitment to the future and make significant investments of our own to add to those of past generations.

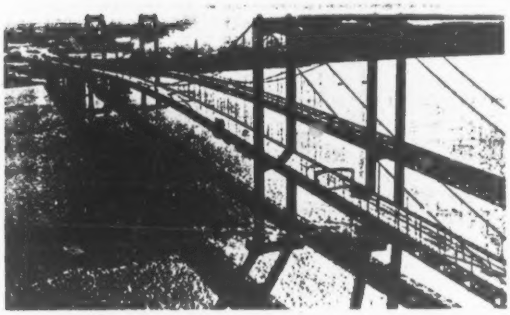
The Council and its staff are proud to report that the Council completed its work within its budget allocation and by the deadline established by the Congress.

Summary of Findings

The quality of a nation's infrastructure is a critical index of its economic vitality. Reliable transportation, clean water, and safe disposal of wastes are basic elements of civilized society and a productive economy. Their absence or failure introduces an intolerable dimension of risk and hardship to everyday life, and a major obstacle to growth and competitiveness.

The Erie Canal; the transcontinental railroads; the great dams and water systems of the west; the airports, seaports, and transit systems that serve our cities; our network of modern highways and soaring bridges—all these are part of this country's great public works inheritance from the generations of Americans who built before us. These massive and sometimes daring achievements supported the growth of the greatest economic power the world has ever known. They have been the envy of other countries and the model for our competitors.

Now that inheritance is in danger.



After two years of study, the National Council on Public Works Improvement (the "Council") has found convincing evidence that the quality of America's infrastructure is barely adequate to fulfill current requirements, and insufficient to meet the demands of future economic growth and development.

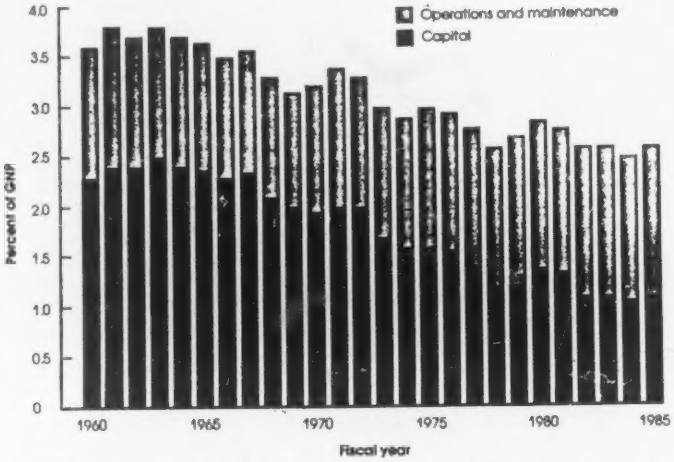
And unless we dramatically enhance the capacity and performance of the nation's public works, our own generation will forfeit its place in the American tradition of commitment to the future. Without such an effort, our legacy will be modest at best. At worst, we will default on our obligation to the future, and succeeding generations will have to compensate for our failures.

> *"We're spending our inheritance. You know, we built this freeway system . . . in the '50's and '60's, and we are still trying to make that do for today's needs."*
>
> Secretary Dewey Lonsberry,
> New Mexico Dept. of Highways
> and Transportation
> Council Hearing,
> Los Angeles, July 29, 1987

At present, most major categories of public works in the United States are performing at only passable levels. A few, such as water supply and water resources, remain in reasonably good shape. But others, such as solid waste and hazardous waste disposal, have serious and growing problems. In addition, smaller systems—in all categories and in nearly all regions of the country—face especially acute difficulties.

Part of the problem is financial. Overall investment in public works has slowed in the last two decades in relation to the demands of growth and environmental concerns. We have worn through the cushion of excess capacity built into earlier investments. In effect, we now are drawing down past investments without making commensurate investments of our own. Fig-

Figure 1—Public works outlays as a percent of GNP



Sources: U.S. Office of Management and Budget, *Budget Appendices of the United States*; U.S. Department of Commerce, Bureau of the Census, *Government Expenditure Series*; and *The Economic Report of the President*; for various years.

ure 1 illustrates this pattern of decline in public works spending as a percent of GNP.

With nearly one trillion dollars of public works assets[1] in the United States, reduced spending over the short term does not mean that individual facilities are in imminent danger of collapse, or that particular regions are in immediate peril. However, a declining infrastructure inevitably will jeopardize the productivity of our economy and our quality of life. Failure to reverse this decline will exact a high price for the nation in the future, both in the cost of deferred investment and in reduced economic competitiveness.

Therefore, the Council recommends a national commitment, shared by all levels of government, the private sector, and the public, to vastly improve America's infrastructure. Such a commitment could require an increase of up to 100 percent in the amount of capital the nation invests each year in new and existing public works. In 1985, this amount was approximately $45 billion.

Dramatically expanding current capacity or doubling the rate of capital spending is not an absolute requirement in all infrastructure categories at all levels of government, or in all regions of the country. However, an increase in capital spending of this magnitude is an important and achievable goal for the nation as a whole by the end of this century. For some categories, such as hazardous waste disposal, an even greater effort may be warranted.

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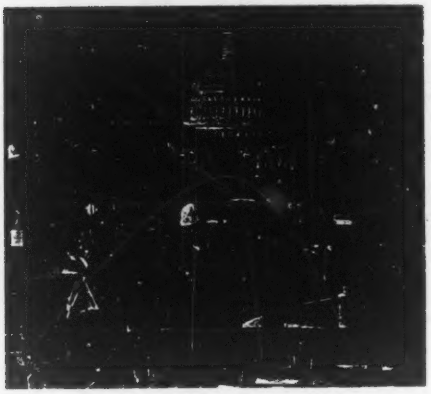
[1] This represents the approximate cumulative depreciated value of the public works facilities in the Council's purview. These include: highways, mass transit, aviation, water resources, water supply, and wastewater, solid waste and hazardous waste disposal. Public works can be interpreted more broadly to include communications, energy facilities, schools, hospitals, prisons, and parks. In an effort to target its resources, the Council has limited its primary focus to transportation, water, and waste disposal issues. Nevertheless, a considerable portion of its research findings and policy conclusions may apply to other areas.

A strategy to upgrade America's infrastructure must incorporate other tactics in addition to increased investment. **Thus the Council also recommends:**

- **Clarification of the respective roles of the federal, state and local governments in the construction and management of infrastructure to focus responsibility and increase accountability;**
- **Steps to improve the performance and efficiency of existing facilities;**
- **A rational capital budgeting process at all levels of government;**
- **Strong incentives to ensure adequate maintenance and, where appropriate, adopt new technologies; and**
- **More rigorous and widespread use of low capital techniques for delivering services and meeting service needs, such as demand management, coordinated land-use planning, and waste reduction and recycling.**

Through these measures the nation can make the best use of existing assets. This approach also may help to defer or avoid a significant portion of capital needs and costs that otherwise would be required in the future.

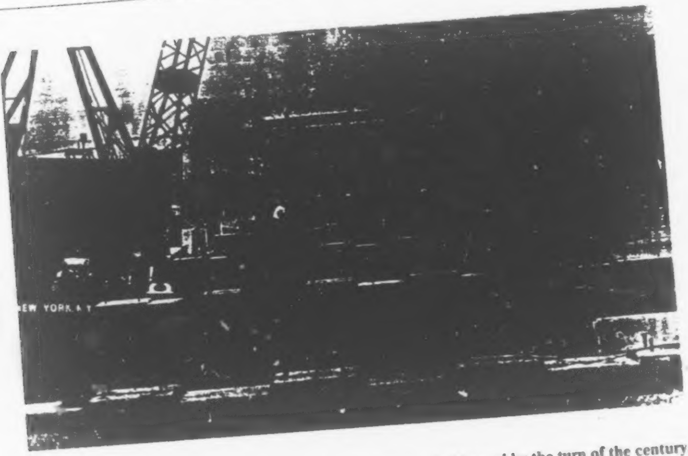


> *"Where in this myriad of problems is the good news? I would suggest that it lies in the opportunity to get government moving before an infrastructure crisis is upon us."*
>
> Michael Deland,
> Regional Administrator, EPA,
> Boston, Massachusetts
> Council Hearing,
> Boston, Aug. 3, 1987

The Council recommends that state and local governments continue to play their traditional leadership roles in the construction and management of the nation's infrastructure. But the Council also believes that the federal government must act as a full and responsible partner on a long-term basis in the national effort to increase and sustain public capital investment.

There is much to set right in America's house. The Council recognizes that an increased investment in infrastructure is just one among many critical claims on the nation's resources. To address this claim and others requires that we reckon first with the growing imbalance between consumption on the one hand and investment and savings on the other. This imbalance, reflected in the federal budget deficit and in other forms of borrowing against the future, affects all federal spending decisions. **The Council supports appropriate actions to redress the imbalance between consumption and savings so that future infrastructure commitments will not be shortchanged.**

The Council believes that infrastructure must rank high among our priorities. We must ensure that our highways and subways can move us swiftly and safely; that our homes, farms, and industries are supplied with ample clean water; that we re-



duce and safely dispose of the increasing volume of poisonous wastes our society generates; and that we provide the structural underpinning for a robust and competitive economy.

To reach this goal by the turn of the century, we must start now to rebuild what we have neglected, to repay where we have borrowed, and to invest again in our future and our children's future.

Joseph M. Giglio

Joseph M. Giglio
Chairman, New York, New York

Peter C Goldmark

Peter C. Goldmark Jr.
New York, New York

Lowell B. Jackson

Lowell Jackson
Aurora, Colorado

Freeman Holmer

Freeman Holmer
Eugene, Oregon

Frieda K. Wallison

Frieda K. Wallison
Washington, D.C.

Reinvesting in America

Sharply upgrading America's infrastructure is an ambitious goal. It cannot be achieved in a short period. Our infrastructure problems are manageable, but only if we begin to mobilize our resources now. These problems cannot and should not be solved through a crash program. Rather, success requires that all levels of government and the private sector dedicate themselves to a sustained effort.

This effort should focus on the effective capacity of our infrastructure systems—the level and quality of public services provided by each category. No single approach by itself will be adequate. More money alone will not suffice. More effective management alone will not get the job done. Technology will not save the day. The complexity of these systems and their attendant problems demand a broad-based strategy.

> *"... there is no 'quick-fix' for the problem. It's much more likely to be solved—eventually—through deliberate remedial steps rather than through a fast, dramatic 'conversion' of practices and attitudes."*
>
> Mayor George Latimer,
> City of Saint Paul, Minnesota
> Letter to the Council,
> June 22, 1987

Rating America's Infrastructure Performance

To determine where we must go, we first must assess where we are. The current condition of the nation's infrastructure is hardly encouraging. If our public works were graded on an academic scale, their recent performance would earn a scant "C"—barely adequate to support current demands.

Yet a single grade cannot reflect the variability of performance by category or within categories. For example, municipal refuse is collected with some success, but limited landfill capacity is making disposal more expensive and less effective.

The report card on the following page provides an overview of the performance of eight categories of public works. By identifying recent program changes and outstanding policy concerns, it also highlights opportunities for improvement.

> *"The public needs to understand that major public works projects have a tremendous lead time, especially if they are located in a metropolitan area or involve controversy. It took more than 20 years from inception to the opening of Interstate 66 from the Capitol Beltway to the city of Washington, D.C."*
>
> Albert A. Grant, P.E., President,
> American Society of Civil Engineers

REPORT CARD ON THE NATION'S PUBLIC WORKS

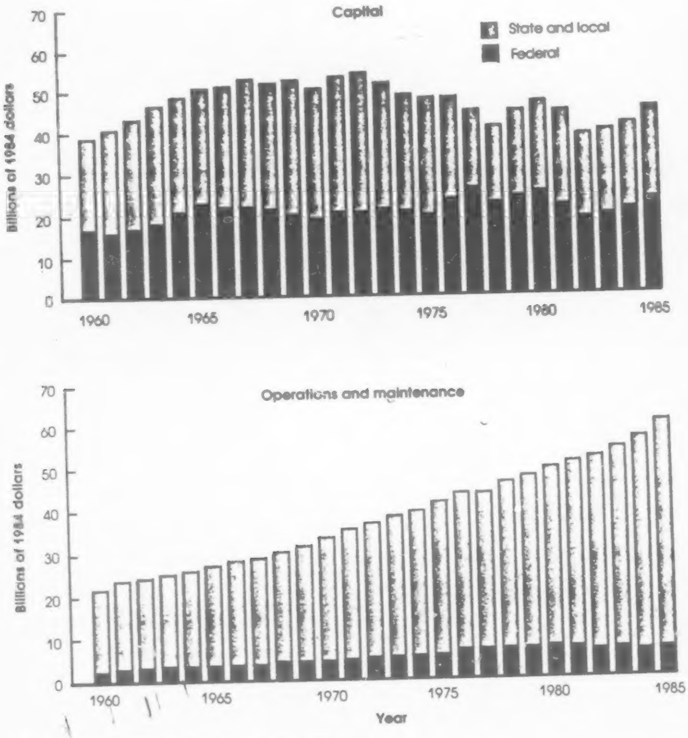
Subject Category	Grade	Successes/ Recent Changes	Problems/ Future Weaknesses
HIGHWAYS	C+	Federal and state gas tax increases have injected new capital into the system. This, along with inceased O&M spending, has improved pavement conditions. However, quality of service in terms of congestion is declining.	Spending for system expansion has fallen short of need in high-growth urban and suburban areas. Many roadways and bridges are aging and require major work. Needs of most rural and smaller systems exceed available resources. Highway Trust Fund has a sizeable cash balance.
MASS TRANSIT	C−	Federal capital grants have helped improve quality of service in some areas, but overall productivity of the system has declined significantly. Growth of transit vehicles is double the rate of increase in ridership. Diverting people from cars is increasingly difficult.	Mass transit is overcapitalized in many smaller cities and inadequate in large, older cities. Systems rarely are linked to land-use planning and broader transportation goals. Maintenance has been erratic and inadequate, especially in older cities.
AVIATION	B−	In general, the aviation system has handled rapid increases in demand safely and effectively. However, service has begun to decline in the face of increasing airport and airspace congestion as a result of strong traffic growth. The air traffic control system is currently undergoing a $16 billion modernization.	Congestion is the system's primary problem. Despite recent increases in authorizations, sizeable cash balance remains unspent in the Airport and Airway Trust Fund. The air traffic control system needs substantial upgrading to maintain safety.
WATER RESOURCES	B	Water Resources Act of 1986 made cost-sharing mandatory for many types of water projects. This change should improve project selection and reduce overall project costs.	Cost-sharing will improve efficiency but also increase local costs of water projects. Poorer communities may find it difficult to finance projects. Implementation is often excessively slow and cumbersome.
WATER SUPPLY	B−	While regional performance varies, water supply stands out as an effective, locally-operated program. Strict new standards created by the 1986 Safe Drinking Water Act will require drastic increases in water rates over the next decade.	Many public water systems suffer from pricing below costs, inability to meet purity standards, or source contamination. Storage and distribution systems are deteriorating in some older cities and supplies are limited in some parts of the West and several cities along the East coast.
WASTEWATER	C	Over 75% of U.S. population is served by secondary treatment plants. Shift from federal grants to state revolving loans may improve efficiency of plant construction. Broadened focus on nonpoint source pollution and groundwater contamination may accelerate progress toward cleaner water.	Despite $44 billion federal investment in sewage treatment since 1972, water quality has not improved significantly. This is due in part to uncontrolled sources of pollution, such as run-off from farmland and roadways. Overall productivity of secondary treatment facilities is declining, resulting in an increase in water quality violations.
SOLID WASTE	C−	Testing and monitoring of solid waste facilities are more rigorous as a result of tougher environmental standards. Waste-to-energy technology is growing as alternative to landfills. More aggressive waste reduction, separation, and recycling efforts are beginning at the local level. However, few states have moved boldly on these measures.	Nation faces significant costs of adequate and safe facilities. Limited data suggest trends toward fewer but safer landfills, rapid growth in resource recovery, and little progress toward waste reduction. Public opposition to siting all types of facilities is a major problem.
HAZARDOUS WASTE	D	Funding for site clean-up has increased five-fold since 1986, but progress has been slower than expected. Only a small fraction of the two tons of waste per capita produced in America each year is being treated safely. Major challenge is still ahead of us.	Nation has forfeited much of its opportunity to reduce waste before it is produced. Waste control legislation promotes "end-of-pipe" rather than source reduction solutions. Congressional mandates and schedules may be overly optimistic, given administrative resources. A massive backlog of poisons and needed cleanup projects faces the nation.

Current Spending on Public Works[2]

Capital investment represents front-end, long-term resources committed to the plant and rolling stock that provide public works services. Measured in 1984 dollars, state and local capital investment peaked in 1972 at $34 billion; annual federal outlays for capital, however, peaked at $25 billion in the late 1970s. This trend is charted in Figure 2.

Spending for operations and maintenance (O&M) is key to the overall longevity and efficiency of public works capital assets. In the aggregate, spending for O&M has continued to grow at a rapid rate since the 1960s (from $21.6 billion in 1960 to $56.5

Figure 2—Government outlays for public works



Source: Apogee Research, Inc., Government expenditure databases billion in 1984), as also shown in Figure 2. Underlying this trend was a small decline in federal operating outlays since the mid-1970s and a substantial increase in local O&M outlays over the entire 24-year period.

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[2] All dollars are expressed in constant 1984 dollars, unless otherwise noted in the text.

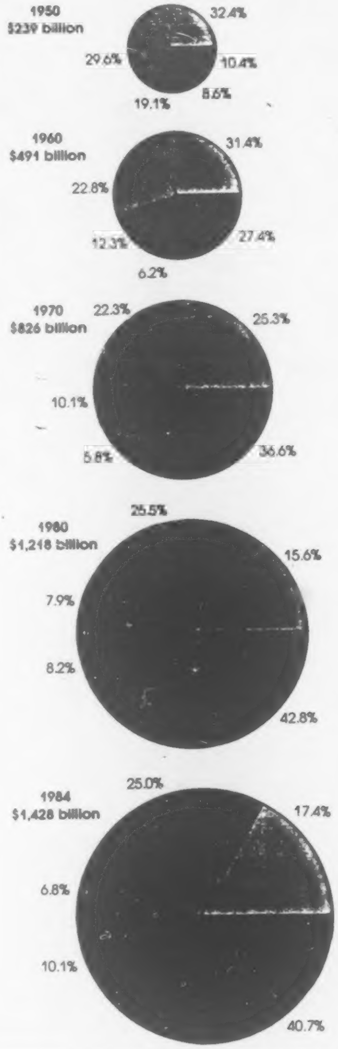
Public works spending patterns are of particular concern when viewed in relation to other measures of economic activity. For example, total public spending on infrastructure has dropped from 3.6 percent of the gross national product (GNP) in 1960 to 2.6 percent in 1985. While spending on operations and maintenance has remained a constant share of GNP, capital spending has dropped from 2.3 percent of GNP in 1960 to 1.1 percent today. The relative share of public works spending at all levels of government has declined drastically from nearly 20 percent of total expenditures in 1950 to less than 7 percent in 1984, as shown in Figure 3. During this same period, government spending for welfare and education increased from 10 percent to over 40 percent of total expenditures.

> *"There is . . . growing concern at the state and local level that . . . given competing demands for funding at the local level for education, health, welfare and public safety programs, the public works infrastructure may indeed experience severe deterioration in the coming years."*
>
> Harout Sanasarian, Supervisor
> Milwaukee County, Wisconsin
> Council Hearing,
> Indianapolis, July 12, 1987

Figure 3—All government spending, 1950–1984 in 1984 dollars

1950	$239 billion
1960	$491 billion
1970	$826 billion
1980	$1,218 billion
1984	$1,428 billion

- ▧ Defense
- ☐ Nondefense discretionary
- ■ Public works
- ■ Interest on general debt
- ■ Public welfare/education



Source: Apogee Research, Inc.

Public works investment is growing more slowly than private capital investment. Private-sector capital investment increased by about 51 percent between 1975 and 1985, but public works investment fell by more than 6 percent over the same period. Figure 4 shows the decline in public works spending per dollar of new private capital put in place.

Economic Prognosis

What do these trends mean for the health of the economy? The level of public works spending is only one indicator of the quantity and quality of service. However, we do know that public investment generally increases the productivity of private investment. Thus the growing imbalance between public and private investment means that we probably are not getting as much value as we could for every private investment dollar. The resulting loss in productivity limits the growth of the economy and our ability to compete in world markets.

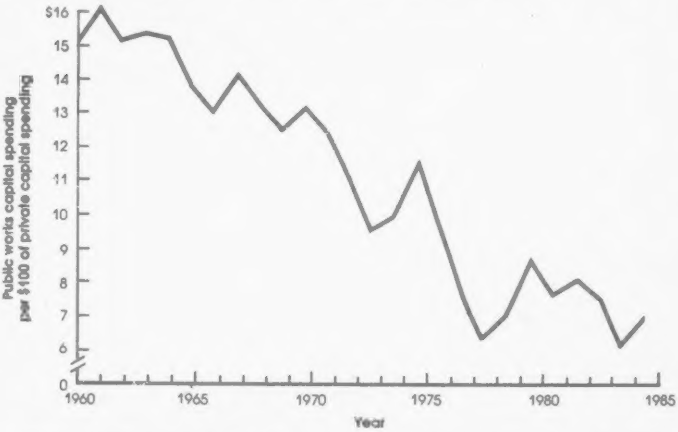
In light of these spending trends and the concerns about future performance outlined above, it is clear that substantially more must be done—and we must start soon.

> *"For the sake of our nation's future, we must provide the funds necessary to maintain and improve roadways and bridges. These are the networks essential for our economic survival."*
>
> James Sullivan, President,
> Greater Boston Chamber of Commerce
> Council Hearing,
> Boston, Aug. 3, 1987

Elected officials and the public at large must recognize that capital expenditures are not the only cost of public works; rather, the expense incurred through delays in providing needed services, added to the value of lost economic opportunities, often can exceed direct budget costs.

> *"The long pattern of disinvestment and a deteriorating infrastructure have eroded our capacities to sustain economic growth—growth which is translated directly into jobs for Americans."*
>
> The late
> Mayor Harold Washington
> City of Chicago
> Council Hearing,
> Chicago, Sept. 30, 1987

Figure 4—Comparison of public works capital spending to private capital spending



Sources: National Council on Public Works Improvement calculations based on the *Economic Report of the President*, January 1987, Appendix B, and Apogee Research, Inc., Government expenditures database.

Our current level of capital investment is barely enough to offset annual depreciation, much less meet new demands. The U.S. Department of Commerce estimates that infrastructure use by industry alone will increase by at least 30 percent over the next ten years as a result of economic growth, the dispersion of population and economic activity, and technological and structural changes. Infrastructure capacity must keep pace with this increase while still maintaining the current quality of service. Better service—reduced congestion, improved water quality, higher safety levels—will require even greater capacity expansion, as well as extensive operational improvements.

> *"The condition of our transportation infrastructure is a critical factor in determining our nation's productivity and our ability to compete and survive in today's world market. We face widespread economic decline if we allow our tremendous highway infrastructure investment to deteriorate."*

Commissioner Leonard Levine,
Minnesota Department of
Transportation
Council Hearing,
Chicago, Sept. 30, 1987

> *"Currently the cost of congestion in Los Angeles County is about 485,000 hours per day of wasted time by our residents or people driving through the county. That converts . . . by our estimates to a minimum of about $507 million per year in wasted time, and about 72 million gallons of gasoline . . . just in our county."*

Rich Richmond, Executive Director,
Los Angeles County
Transportation Commission
Council Hearing,
Los Angeles, July 29, 1987

While a sound infrastructure does not guarantee future prosperity, long-term economic growth cannot be achieved without it. Economic efficiency and public health both are linked inextricably to adequate transportation, water quality, and waste disposal services. In addition, infrastructure investment directly supports additional economic activity. For every public dollar spent on an annual basis to build and maintain our network of roads, streets, and bridges, the private sector spends $15 to move people and goods. For every public aviation dollar, private firms and individuals spend nine.

If we spend too little on public works or if we invest in inefficient projects, society loses more than the direct public cost. In the long run, our ability to compete in the international economy will be weakened, and our standard of living will suffer.

Finding the Money

Much of the discussion about public works in recent years has focused on choosing appropriate finance mechanisms—e.g., revolving loan funds, intergovernmental grants, tax-exempt debt techniques, or various forms of privatization. While these options may differ in terms of the attractions they offer to public officials, they all draw on two basic sources of funds—*general tax revenues* and *user fees*.

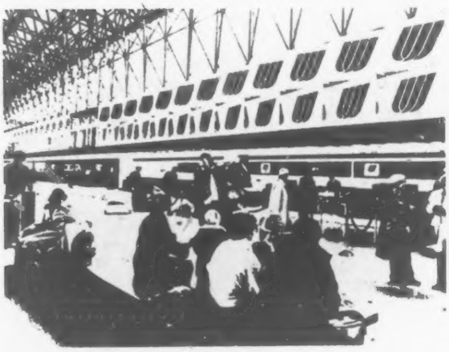
Mobilizing adequate financing to meet our current and future public works needs requires participation by all levels of government. **The Council endorses the following principles to guide this effort:**

- **Users and other beneficiaries should pay a greater share of the cost of infrastructure service.**
- **The federal government should be a reliable partner in financing public works.**
- **States should develop comprehensive infrastructure finance strategies.**
- **Local governments should give budgetary priority to funding the maintenance of existing facilities.**

Emphasis on the Beneficiaries

Today almost 75 percent of public capital spending on infrastructure is derived from users. Yet only about 50 percent of spending on operations and maintenance comes from this source. Significant elements of transportation, water supply, wastewater treatment, and solid and hazardous waste systems serve identifiable consumers on a continuing basis. Use can be measured and priced; those who do not pay can be excluded from services. Linking financing to use can produce a steady and predictable revenue stream, encouraging better maintenance, rehabilitation, and replacement.

> *"New strategies like public-private partnerships will help. So will federal initiatives. . . . But what I think is really needed first is a national consensus. We need to better define the scope of the problem—what are the specific needs for all levels—and then identify what resources can be marshalled and by whom."*
>
> Mayor Don Erickson,
> Cheyenne, Wyoming
> Council Hearing,
> Los Angeles, July 29, 1987



The Council recognizes important limitations to the user fee principle. Many smaller communities lack the financial base necessary to finance a facility—especially when new capital investment is required. Fees for certain types of essential services, such as water supply, sewage treatment, and solid waste disposal, also can be excessively expensive for lower income residents or hard-to-serve areas.

Options to address these problems may include guarantees or insurance for small-issue debt; state bond banks that combine small bond issues into larger, more creditworthy statewide issues; selected increases in grants targeted to smaller facilities or those serving lower income areas; and re-gionalization of services to achieve economies of scale. Providing a threshold level of service and a safety net in these instances also may require general revenues to supplement user fees.

Public works produce both direct and indirect benefits. For example, a mass transit system benefits the transit riders as well as the motorists who travel in the area. In addition, mass transit often benefits business and commercial interests. Thus, the cost of transit development or expansion should be borne by all three groups.

> *"Twenty years ago developers looked almost entirely to the public sector for infrastructure. Today with increasing population and migration of people and businesses to the cities and surrounding counties of Nashville growing so much faster, the public sector can no longer provide total infrastructure needs. The future must be a joint effort."*
>
> George Volkert, President,
> Southeast Venture Company,
> Nashville, Tenn.
> Council Hearing, Nashville, June 9, 1986

User fees may prove inadequate for major new investments in infrastructure technology and economic development. Such projects have few immediate or easily identifiable beneficiaries. Instead, they represent long-term commitments to the future, and rightfully are a matter of common responsibility, to be financed out of general funds or a user fee base that includes both present and future beneficiaries.

The Council endorses the general principle that developers should pay an equitable portion of the cost of new facilities necessary to service commercial, industrial, and residential development. State and local officials should exercise due care to see that the allocation of such costs is fair and reasonable and does not result in undue private influence over public development policies and priorities. Further, it should be recognized that developer fees and exactions will have an impact on the cost and availabilty of housing.

The Council urges that federal user fees paid in good faith by beneficiaries to preserve and protect public works systems be spent for that purpose. The accumulation of unspent balances in the federal highway, transit, aviation, and waterways trust funds—nearly $24 billion in the 1987 budget—is at odds with this principle. **The Council supports a determined, incremental effort to reduce these balances—in line with responsible management and planning—so that the funds can be used for necessary infrastructure improvements.**

Federal Partnership

Between 1960 and 1975, federal grants-in-aid as a portion of total state and local capital spending remained relatively stable at about 33 percent (Figure 5). In the late 1970s, federal aid rose to more than 50 percent; since then it has leveled off at 40 to 45 percent. These patterns reflect a decline in capital spending by state and local governments as well as shifts in federal grant policy.

In the realm of infrastructure finance, the federal government traditionally has focused on providing public works capital. Because of its limited involvement in maintenance and operations, the federal government accounts for less than 30 percent of all public works spending.

The Council urges the President and the Congress to recognize the importance of maintaining a continuing federal role in infrastructure finance. Intergovernmental aid still is necessary to launch major projects of national interest, or to help governments with limited fiscal capacity. However, some changes in the form of federal spending may be necessary to accommodate shifting federal, state, and local roles and relative fiscal capacities.

Whatever form federal assistance takes, it should offer state and local governments:

- Stability over several years to aid long-range planning;
- Flexibility in the use of funds through such mechanisms as block grants; and
- Incentives for increased efficiency and improved maintenance.

In addition, the federal government should exercise restraint in adopting legislation that would limit the revenue-raising capacities of state and local governments.

Federal tax policy also has a significant impact on infrastructure finance. For example, the Tax Reform Act of 1986 drastically limits arbitrage earnings on borrowed funds and restricts the use of municipal bond proceeds for quasi-public projects by imposing ceilings on allowable issues. These and other provisions are expected to limit the growth of tax-exempt bonds, and to increase state and local borrowing costs. The law also lengthens depreciation schedules and repeals investment tax credits, which will increase the cost of joint development of certain public works with the private sector. In combination, the provisions of the 1986 law may impede the financial plans of state and local governments, reduce their fiscal capacity, and limit their ability to finance necessary improvements.

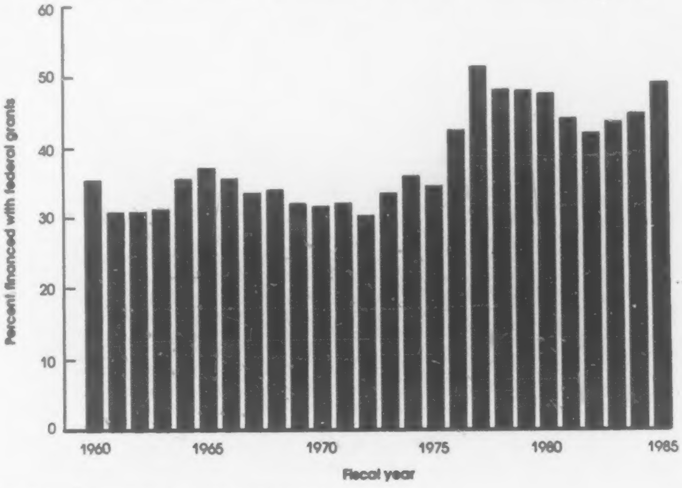
The Council urges the President and the Congress to pay close attention to the effects of tax reform, and to remove unwarranted limitations on the power of state and local governments to finance public works.

State Strategies

Although a number of states have instituted innovative financing programs, the state share of overall spending on infrastructure dropped from 32 percent in 1970 to 23 percent in 1985. At $25 billion annually, state

> *"I think we have seen the end of . . . massive amounts of federal dollars returning to local governments through federal revenue sharing and any grant program. I think at the state and local levels we must . . . go to Washington and ask for programs and policies that are feasible in light of the changed fiscal circumstances."*
>
> Ronald Bean, Executive Director, Illinois Development Finance Authority
> Council Hearing, Chicago, Sept. 30, 1987

Figure 5—Percent of state and local public works capital spending financed with federal grants



Source: Apogee Research, Inc., Government expenditures databases.

> "We as local communities are property tax dependent. We have no access . . . and it is true in most all New England states, to any other forms of taxation."
>
> Pam Plumb, City Council Member, Portland, Maine, and 1988 President of the National League of Cities
> Council Hearing,
> Boston, Aug. 4, 1987

taxes and fees now finance less than one-third of expenditures on state and local public works programs.

While localities are under pressure to fund an increasing portion of total public works spending, often they must contend with state restrictions on taxation or bonding. For example, as of 1985, 31 states had imposed specific property tax rate limits on local governments. Six states had either constitutional or statutory limits on the total amount of revenues that local governments could collect annually.

The Council encourages governors and state legislatures to examine the impact of such restrictions on state and local public works. Where state constitutional or statutory limitations hinder the ability of the state and local jurisdictions to deliver essential services or adversely affect their credit ratings and finance capacity, states should assume responsibility for either remedying the situation or providing compensatory assistance.

Future Finance Options

The Council has called for a substantial increase in the capacity and effectiveness of the nation's public works. This goal is not attainable unless we first make better use of existing financial resources. In most cases, however, we cannot rely simply on wiser spending; we also must generate additional sources of funding. This burden will fall on all levels of government and involve virtually every category of public works.

The Council supports the concept that the unit of government responsible for service delivery should be the one that levies the fees or taxes to the extent possible and practical. This will strengthen accountability for the cost and quality of public works service. Local governments already bear the lion's share of operating and maintenance costs and a growing portion of capital costs as well. But to carry out their responsibilities, they must have the proper tools, such as taxing and bonding authority and access to the tax-exempt municipal bond market.

> "One point seems to be very clear. The people are willing to dig into their own pockets to pay for better roads, more schools, clean water, expanded airports, improved transportation, and the items which help shape the quality of life in the Golden State."
>
> Don McGrew, President,
> Griffith Company,
> Long Beach, California
> Council Hearing,
> Los Angeles, July 29, 1987

It is not appropriate for the Council to propose a specific legislative program of new fees and taxes to finance public works improvements. The most equitable and efficient mechanisms will depend on the type of infrastructure problem being addressed and on local conditions, traditions, and institutions. These trade-offs are made through the political process at all levels of government. The menu of possible revenue sources listed in Table 1 provides a starting point for assembling such a program.

Many of the options in Table 1 represent simple expansions of existing user fees or related excise taxes. The largest potential sources of funding are motor fuel taxes used by the federal and state governments to support highways and some transit spending, and developer exactions and related fees imposed by many local governments. Local exactions are perhaps the fastest growing means of infrastructure finance, as well as the least well known.

Table 1.—Possible Sources of New Public Works Revenues

Source	Level of Government	Current Rate	Possible Increment	Potential Revenues ($ millions/year)
Motor Fuels Tax				
a) Flat Tax	F,S,L	$0.23/gal[a]	$0.10/gal	$12,000
b) Ad Valorem	F,S,L	(b)	10% of fuel costs	9,500
Repeal Exemptions from Highway Taxes	F	(c)	N.A.	1,000
Heavy Truck Taxes	F,S			1,000
Aviation Ticket Tax	F	8% of value	2% of value	800
Airport Service Charge	L	None[d]	$3/passenger	1,500
Inland Barge Fuel	F	$0.10/gal[e]	$0.10/gal	50
Port Tax	F	0.04% of cargo value	0.06% of cargo value	250
Cash Balances in Trust Fund Cash	F	N.A.	(f)	2,000
Water Supply	F,S	None[g]	$0.10/1,000 gallons	750
Waste-End Taxes	F,S			
a) Generation		None	$5/ton	1,500
b) Disposal —by Hazard		None	$0–$60/ton	2,600
c) Disposal —by Method		None	$4–$25/ton	3,200
Local Impact Fees on Developers	L	(h)	(i)	10,000-15,000

NOTE: Revenue estimates show gross receipts and have not been adjusted for potential reductions in other taxes. These offsets could reduce gross receipts by as much as 25 percent.

SOURCE: Apogee Research

[a] The current federal tax is 9 cents per gallon of gasoline. State taxes average 14 cents per gallon. The federal government taxes diesel fuel at an additional 6 cents per gallon.

[b] Some states currently collect sales taxes on motor fuel.

[c] State and local vehicles, transit buses and users of gasohol are exempt from certain federal and state taxes despite the wear and tear they cause on roads and bridges.

[d] This charge, commonly referred to as a "head tax," currently is prohibited by federal law.

[e] Scheduled to increase to 20 cents per gallon by 1995.

[f] Assumes the current trust fund cash balances will be used over the next ten years.

[g] None at the federal level; Washington is one of the few states with a water excise tax.

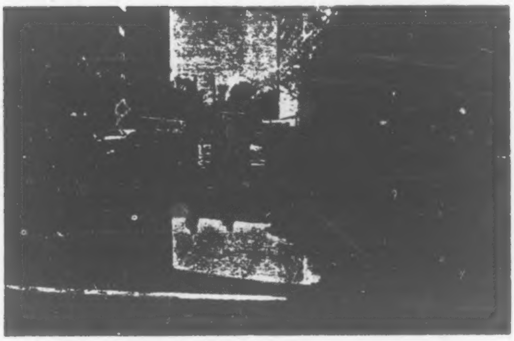
[h] Many local governments already impose some form of negotiated fee for the infrastructure costs resulting from new development.

[i] Assumes that impact fees and related techniques are increased to equal 20 to 30 percent of capital spending. Potential revenues are not likely to be realized until the mid-1990s.

Sharpening Accountability for Infrastructure

Dependable, high-quality infrastructure is not the product of money alone; building and maintaining public works requires a shared vision, commitment of time and energy, and the skills of people throughout the public and private sectors. Historically, such consensus often has been a local or regional phenomenon in America. The result is a system that is highly decentralized and subject to continual change. Each community has its own laws, traditions, and other characteristics that govern the way it apportions responsibility and resources for public works.

On the whole, this system has worked well in providing public works facilities and services for a large number of communities. But too often, when problems arise, ultimate responsibility among various levels of government is not understood clearly by either the public or its leaders. When the solutions are costly, complex, and controversial, or involve a wide range of players, our tendency, as individual communities and as a nation, is to stall and point our fingers at the "other guy" until we reach a crisis. By this time we generally have foregone the most sensible and inexpensive options. Last summer's story of the Long Island garbage barge wandering forlornly around the Caribbean is one such example. Most of its cargo was used paper—a commodity that could have been recycled for sale in many parts of the world. In the end, accountability was fixed back on the community that generated the garbage, but by then the cargo was waterlogged and without value.



The Council urges that the roles of the federal, state, and local governments be clarified to help boost the performance of the nation's public works.

In general, the Council believes the federal government should continue its primary role in hazardous waste disposal and cleanup, air traffic control, inland waterways, highways of national significance, intermodal freight transportation, minimum performance standards for environmental protection, major capital investments for flood control and shoreline protection, and the overall coordination of water resource programs.

> *"There is no perfect solution to solid waste disposal. . . . Everything we do will have some minor impact. . . . It must be disposed of and that place is inevitably in somebody else's backyard, and that is one of our problems."*
>
> Frank Borchardt,
> Executive Vice President,
> HDR Techserv,
> Omaha, Nebraska
> Council Hearing,
> Chicago, Sept. 30, 1987

In turn, states should have lead responsibility for highways of statewide significance, non-federal dam safety, major capital financing of wastewater treatment, airport system planning, and the siting of waste disposal facilities.

Local governments, or in some cases regional authorities, should have primary responsibility for local streets and roads, public transit, individual airports, water supply systems, ports, urban stormwater, wastewater treatment facilities, and solid waste disposal. In many instances, these services may be financed and operated by private firms through agreements with local jurisdictions. Opportunities for private participation should be considered actively by all levels of government but should not be seen as a panacea.

The impact and importance of most public works are not neatly locked within the boundaries of any given jurisdiction. One community's failure to provide good roads or adequate sewage treatment may hinder all others in the vicinity. Stewardship of the infrastructure as a whole demands some degree of accountability by all levels of government. However, in a dynamic and fractionated federal system such as ours, accountability can be measured more usefully against general principles than rigid standards.

The Council believes that state and federal infrastructure policy should support local self-sufficiency to the greatest extent possible. This means that:

(1) **Federal and state statutes should be far clearer and more rigorous in specifying who is responsible for doing what, and by what deadline.** Many laws and program guidelines governing complex projects contribute to delay and lack of accountability by failing to set timely deadlines for reviews. Nor do they specify who will resolve conflicting advice or opinions when many different agencies are involved. The immense difficulties of siting solid and hazardous waste facilities and the long, costly delays associated with port and navigation projects are reflections of this bureaucratic equivocation;

(2) **Federal and state public works mandates should be considered carefully and allow cost-effective methods of compliance rather than rigid technical requirements.** For example, in older urban areas, "dial-a-ride" services can provide equivalent mobility for the physically handicapped more cost-effectively than retrofitting all transit vehicles;

(3) **Rules governing state and federal programs should recognize the distinct financial and managerial needs of small and rural governments;**

(4) **States should seek to promote cooperation among local jurisdictions, as well as between state and local government.** State advisory councils on intergovernmental relations, regional planning commissions, councils of government, and interlocal agreements are useful mechanisms to achieve this goal; and

(5) **The federal and state governments should address the need for adequate technical information and expertise when they impose responsibilities on local government.** "Circuit riders" or other forms of technical assistance and training should be considered where appropriate.

STATEMENT OF THE

NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS

SUBMITTED FOR THE RECORD AT HEARINGS ON

INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

BEFORE THE

SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM AND THE
DISTRICT OF COLUMBIA

COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
May 4, 1989

The National Association of Towns and Townships (NATaT) is pleased to submit this statement concerning intergovernmental solutions which must be brought to bear on rebuilding the nation's infrastructure. NATaT represents more than 13,000 units of general purpose local governments across the United States. These mostly small, mostly rural communities are typical of the majority of the nation's 39,000 general purpose governments, Mr. Chairman. In approaching the infrastructure issue we must remember that we are a nation of small communities Only fourteen percent of the general purpose governments in the United States below the state level serve populations over 10,000, while 72 percent of such governments serve populations of less than 3,000, and fully half of all such governments serve communities with less than 1,000 peop

These localities are significantly different than their urban and suburban counterparts in terms of staff and other resources; most have no paid staff accountants or lawyers, no professional city managers. There are no environmental engineers on the payroll, no grantspersons to secure intergovernmental aid, no major companies to invest in large public/private enterprises. These communities are the overwhelming majority of the localities in the federal-state-local partnership. They succeed on the sheer will of their dedicated public servants -- their locally elected leaders who for the most part volunteer their time and expertise as a service to their friends and neighbors in the community.

The Importance of Infrastructure in Small Communities

Mr. Chairman, small governments such as those we represent have major responsibilities in the three primary infrastructure areas which you are reviewing today: transportation, water, and solid waste disposal. Since most of the governments in the United States are small, it should come as no surprise that the task of meeting infrastructure needs rests in large part with very small communities -- those with the least ability to finance the building and maintenance of roads, bridges, water and sewer systems, and solid waste disposal facilities.

Small governments have the responsibility for the vast majority of road mileage, and tens of thousands of bridges across the United States. They have major responsibilities for providing and/or monitoring drinking water; addressing the problem of wastewater, and for meeting the stringent standards set by environmental regulations -- which for the most part have been written without regard to the resources available in small and very small governments.

And of course, the small local governments -- ten of thousands of them -- are responsible for solid waste disposal, through joint agreements with other jurisdictions, as contractors with private firms, or as principals who site and maintain solid waste disposal facilities with all the attendant problems.

The Problems

Roads and Bridges

As reported by the National Council on Public Works Improvement, the nation's infrastructure is deteriorating at an alarming rate. Over 60 percent of the nation's paved roads and a quarter of the Interstate Highway System is in need of resurfacing, according to the Federal Highway Administration (FHWA). Forty-five percent of the nation's bridges are considered obsolete or structurally deficient, and a large number of those are in small communities; on the average, one bridge collapses every two days, Mr. Chairman -- or to think of it another way, three bridges have collapsed since Monday, and another one is about to go.

More than 80 percent of the national road system is in rural areas, and nearly 70 percent is the responsibility of local governmental units; but only 20 percent is eligible for federal highway funds. Four hundred seventy thousand bridges of 20 feet or more in length have been inventoried, not to mention thousands more which are smaller. According to a recent study by USDA's Office of Transportation, the main responsibility of local governments in this area is the off-system bridges -- those not located on a Federal-Aid highway. "In 1986," the study reports, "a total of 279,091 bridges (59.4 percent) were not on the Federal-Aid system and, thus had to be financed from State and local funds." There are 9,946 such bridges in your own State of Tennessee, Mr. Chairman; 4,079 in Michigan; 1,272 in Maine; 10,204 in Pennsylvania; and 15,915 in Ohio, for example -- and those are only the inventoried bridges at least 20 feet in length.

Posted bridges in rural areas pose an enormous problem, not only for local communities but for the nation as a whole. In Pennsylvania, for example, local steel companies spend over $1 million a year detouring around the bridges which cannot support the weight of their trucks, according to the

Pennsylvania DOT. By projecting that $1 million for one industry in one state to thousands of industries in 50 states, the enormity of the economic implications becomes apparent.

Local roads also play an important role in the national economy. Some of them are farm-to-market roads; but beyond that traditional function, the role of the local road system has been significantly altered. A decreased railroad network along with changing demographics of truck transportation -- larger loads, heavier trucks -- has increased the importance of many local rural roads. According to the Federal Highway Administration, most truck vehicle miles of traffic (VMT) occur on rural roads off of the Interstate system -- and that majority will triple by the year 2020. In 1985, trucks with six or more tires logged over 30 million VMT off the Interstate system on urban roads, and 47 million VMT on rural roads off the Interstates. FHWA projects that in 2020, urban truck mileage -- again, off the Interstate -- will increase by 30 million VMT, while rural mileage will increase nearly three times that -- by nearly 90 million, to a total of 137,131 million VMT. (See chart attached). These statistics underscore the fact that the growing importance of local and rural roads to the national economy as a whole cannot be ignored.

Water and Solid Waste

The other two categories under discussion today -- water and solid waste -- are regulated by the Environmental Protection Agency (EPA), which itself admits that environmental requirements weigh most heavily against the smallest communities. Small governments, especially those below 3,000 in population (again, nearly three-fourths of all U.S. general purpose governments), find many barriers to financing, building and maintaining facilities at the level mandated by Congress and EPA. In many cases, such barriers are impossible to overcome -- leaving local officials with enormous liabilities and their citizens unprotected. Solid waste disposal looms large on the horizon for small governments. Issues such as municipal landfills and disposal of ash and sludge, will require innovative approaches on the part of federal regulators if they are to be realistically addressed. Not only is it a question of costs of maintaining appropriate facilities in many small communities, but also of whether such facilities can be built at all, given that part-time local officials may not have the level of expertise which will enable them to negotiate successfully with state and federal agencies, lenders, or compete for loans, grants, or other financing.

Small Communities -- Failures, or Keys to the Future?

Without adequate infrastructure, small communities cannot compete. The state of our infrastructure is a serious problem for our nation as a whole; for small communities, it is a matter of survival. Infrastructure is our tie to the outside world; the sledge hammer which breaks down walls of isolation and allows the world to connect. It can also play a key role in creating economic opportunity -- not only for small communities, but for all of America's citizens.

There are major changes at work across this country. Entrepreneurs, service industries, and corporate entities are reaching out to take advantage of emerging technology which enables them to do business anywhere; to move out of large metropolitan areas to towns and villages where the cost of living is lower and the quality of life is higher. The public is ahead of the curve on this one, Mr. Chairman; already investment bankers operate from small towns rather than from New York City; publishing houses, insurance companies, and accounting firms, have moved to small communities; free-lance consultants, data processors, and other service providers are moving back out to the country. And it is happening almost faster than we can recognize.

A Mixed Blessing

The potential of this rural renaissance can be viewed as a mixed blessing. On one hand, it would alleviate congestion and subsequent pressure for our urban centers by creating new opportunities in rural America. On the other hand, rural infrastructure problems will grow greater with new demands, reaching beyond the traditional categories under discussion today. We need to address telecommunications technology; the tremendous demand for fiber optics and effective two-way interchanges not only in high density areas, but throughout the United States. And it means that the needs of our rural health care system -- hospitals, clinics, and emergency medical services -- demand an even higher level of priority.

Financing in Local Government

Mr. Chairman, small governments cannot absorb infrastructure costs alone. In many cases, small community resources are not adequate to meet current needs, much less to develop additional capacity. For the most part, small governments can only rely on the property tax as their chief financing means. As you know, property values in many small communities are declining. Financing mechanisms which are commonplace in larger communities are not always available to small governments, and economies of scale work against them. It is not unusual for small governments to hold raffles and bake sales to supplement annual budgets; such fundraising activities take place in thousands and thousands of governments nationwide.

Although user fees have played an important role in maintaining some forms of infrastructure, particularly in the areas of water, wastewater and solid waste, small governments generally are only able to make limited use of this financing technique. Spreading costs on a per capita basis, as user fees do, is not realistic in very small places where the population is too low to keep costs reasonable. Consequently, small communities can only raise a portion of the costs through user fees; the remainder must be subsidized either by intergovernmental transfers or by bond financing.

Intergovernmental Transfers

In recent years, intergovernmental transfers have been only minimally effective in providing support to small town America because they have been so drastically reduced, and because most programs are not designed to take into account the unique circumstances of small governments. Those federal programs which have helped to finance small town and rural America's infrastructure include the Farmer's Home Administration water and wastewater loans and grants, community facilities loans and grants, EPA's wastewater construction grants programs, the Federal Aid Highway System -- primarily the Secondary (Rural) Highway System and Off-Systems bridge program, Appalachian Highway System, and the Community Development Block Grant Small Cities Program.

Over all, programs that were providing funding for rural America have been cut by over 67 percent since 1980. The Secondary Highway System has lost over 60 percent of its funding in the past decade; in this same period FmHA's water and waste disposal grants program lost nearly 75 percent, water and waste disposal loans lost nearly 65 percent, and the community facilities loans have gone down nearly 80 percent. EPA's construction grants program has been cut by over three-fourths in the last ten years; and the Community Development Block Grant Small Cities program lost one-third of its funding in this same period. Since the elimination of the General Revenue Sharing (GRS) program, 80 percent of the general purpose local governments in the United States receive absolutely no federal funding.

THE INTERGOVERNMENTAL ISSUE

Do these reductions mean that the demand on infrastructure has been reduced? No. Do they signal a decrease in federal mandates, allowing local governments to alter requirements and shift priorities? No. Do they mean that local governments are doing better financially, and thus are more able to shift their own resources to fill the void. Obviously not. What these reductions do mean is that the federal/local partnership has been broken -- that the federal partner has not lived up to its responsibility for marshalling national resources to address national issues. Our infrastructure is a national priority.

Not only has the federal government withdrawn its support, it has exacerbated the problems at the local level by building barriers. This is nowhere more evident than in the case of tax-exempt bond financing. Bond issuance is perhaps the most important financing tool presently at the disposal of local governments. Obviously, infrastructure costs -- new construction and expansion in particular-- are big ticket items. Water systems, wastewater systems, solid waste facilities, new bridges and roads -- cannot be funded on the property tax alone. They cannot be funded by user fees. They cannot be funded by bake sales. The federal government has already eliminated the General Revenue Sharing program which for many years was used by small governments to finance major facilities; and, as we have already discussed, most federal aid to small and local government has fallen victim to the budget cutting ax.

Tax-Exempt Financing: the Next Budget Target

In many cases, the only tool left to small and local government is tax-exempt financing. Although this mechanism is not directly available to thousands of very small communities, those which are somewhat larger have been able to use tax-exempt financing to fund their first wastewater systems, to expand these systems to meet new growth demands, and to replace aging systems, which no longer meet federal standards. Such financing is crucial to raising the millions of dollars required for building safe drinking water systems for small and growing communities. And it will become increasing more important as communities -- small and large alike -- begin to face increasingly urgent environmental issues, including new rules and regulations in the areas of solid waste disposal and ground water protection.

Even though it may be the only remaining mechanism for many local governments, tax-exempt financing is under attack. In its rush to find new revenue sources, Congress is considering eliminating this vital tool. Without tax-exempt financing, governments -- small and large alike -- cannot hope to make even a small dent in the nation's infrastructure needs. Water systems, waste facilities, and sewer systems simply will not be built. Bridges will continue to collapse and roads will continue to deteriorate; storm systems simply will not exist; our communities and our neighbors will be placed at even greater risk.

Pay Now or Pay Later

Mr. Chairman, simply put, we can pay now or pay later. Working through a true cooperative partnership which includes the federal, state, and local governments, we can design programs to begin to address our infrastructure needs. Or we can wait until it is a full-blown crisis -- until our communities collapse around us -- and costs to replace and repair will soar beyond our wildest imagination.

There is no way of getting around the costs, and costs will never be lower. The American public trusts their local, state and federal elected leaders to provide leadership, but the federal government is letting them down -- it is playing with smoke and mirrors -- while knowing that it is placing the future of the nation at risk.

RECOMMENDATIONS

There are no easy solutions for this national problem; but there are a number of recommendations that our association suggests to you today.

First and foremost, we urge Congress and the Administration to recognize that rebuilding the nation's infrastructure is a national priority. This critical issue must be considered as such in setting national priorities -- budgetary and non-budgetary policies -- developed by Congress and the Administration. Most importantly, the federal government must assume its share of the responsibility for rebuilding our nation's infrastructure.

In recognizing its responsibility, the federal government must once again acknowledge local governments as partners in providing essential services to America's citizens, and must stop targeting local government -- particularly small local government -- for revenues.

This means that the federal government must work to strengthen and preserve the fiscal capacity of local governments to address the nation's infrastructure problems in all future federal policies. Tax exempt financing must be preserved. Discretionary programs that finance infrastructure must received a new priority. And the Highway Trust Fund must be used for its original purposes -- to repair and maintain our national system of roads and bridges. All trust fund monies must be allocated for their intended purpose, and not held hostage to meet Gramm/Rudman/Hollings targets. In addition, the gasoline tax, which funds our national road network, must continue to be dedicated for highway expenditures; it must not be invaded for deficit reduction purposes. All efforts should be made to fund these programs proportionately to meet this emerging priority.

From a small local government perspective, federal policymakers must rethink federal assistance programs to ensure that funds are targeted for small communities. Federal programs which allocate funds on a per capita basis will never address the critical problems facing many of the nation's smaller communities, because they inherently direct funds away from these communities in favor the nation's larger cities. Formulas that allocate funds on a per capita basis do not belong in any national program that realistically attempts to address a national problem. If a true federal/local partnership is to exist, the federal government must recognize the bias against small communities which has become inherent in our federal assistance system: per capita and tax effort measurements are perfect examples.

Such criteria essentially prevents funding from reaching small communities. Since most small governments have no staff or professional expertise at their disposal, they cannot compete in an assistance system which requires sophisticated grantsmanship skills in order to succeed. Federal criteria should be based on need. Federal agencies should be required to establish outreach mechanisms to provide assistance in the form of planning, technical assistance, and grantsmanship in order to offer small communities the same access to federal assistance which is currently made available to their larger counterparts.

Rethinking national criteria for federal assistance must be done before the Federal Aid Highway program is reauthorized. With the completion of the interstate system by 1991, a greater share of the trust funds must be directed toward local roads and bridges where there is the greatest need. This includes not only country roads, but also roads within our towns, townships, and small communities. Small town America must be brought into the process as we rethink our federal aid highway system; small communities must receive their fair share of these funds, and state government must be required to work with these small communities in any state planning or priority setting for use of these monies.

Finally, Congress and the Administration must recognize that they must begin to assess priorities as they mandate local governments to implement federal policies. We cannot afford to pay for federally regulated requirements in the areas of clean water, safe drinking water, underground storage tanks, storm sewers, flood plain, clean air, hazardous waste, emergency response, and on and on. It is not that we disagree with these objectives, but rather we simply do not have the resources to pay for requirements which are all to often based on unrealistic expectations and a misunderstanding of local capacities. There is absolutely no federal accounting of the total costs to local government for federally mandated national priorities. Mr. Chairman, it is so easy to mandate local governments to do certain things, but impossible at best to ensure that local governments can indeed meet these requirements.

It is for this reason that NATaT began its campaign several years ago to solicit support for a new rationale regulatory process which takes into account the ability of a small local government to meet national mandates and to work these small communities to devise regulations that make sense.
As you know, Mr. Chairman, we believe that the Regulatory Flexibility Act of 1980, amended as we have recommended to the full committee, will begin this rationale federal policy process

Our recommendations for improving the Reg Flex Act would remove the loophole which allows agencies to ignore the Law and would ensure that agencies consider alternatives in establishing national guidelines -- adjusting requirements to local capacities.

In addition, we have also recommended that the General Accounting Office be required to assess current federal efforts to collect data on small governments, to establish national standards for data gathering which allow for the sharing of information and encourages the sharing of data from agency to agency. We also believe that Congress should require reports from federal agencies which assess the cumulative burden of mandates on small governments. These recommendations have been forwarded to the full committee chairman, Senator Glenn. We urge this subcommittee to support our efforts to secure passage of new legislation in this regard.

In addition, we also believe that Congress itself could do a better job at policing new mandates on local governments through using cumulative data when considering new policies and establishing priorities. A process which takes a hard and realistic look at specific proposed policies in the formulation stage -- that is as bills are drafted -- and considers these proposed policies within the context of what small local governments are already expected to do, makes a great deal more sense than the current process.

KEEPING THE DOOR OPEN

In Conclusion, Mr. Chairman, there is a lot more at stake here than the traditional dream of "small town America." By ignoring small communities, the federal government is closing a bright door to our nation's future. If small communities are forced to fail -- if they fade away, and their children continue to migrate to larger communities looking for homes and jobs -- big city infrastructure problems will grow exponentially. If you think New York City has problems now, or Chicago, or Los Angeles -- or Washington, D.C. -- imagine what it would be like if they were the only alternative! It is clearly in the interest of large and small communities alike to preserve the choices, to encourage economic development in rural areas, and to reduce the pressure on the urban infrastructure. Viewing the problem in its entirety -- from the perspective of urban centers, small communities, and the places in between -- our national interest lies in a secure intergovernmental partnership, forming a solid foundation for current and future infrastructure investment.

Mr. Chairman, on behalf of tens of thousands of small governments across this nation, thank you for your concern and your support. We applaud you and the committee members for recognizing the importance of this issue and for scheduling this hearing today. NATaT appreciates the opportunity to present this statement, and we would be happy to respond to any questions.

Thank you.

STATEMENT FOR THE RECORD
BY ROBERT B. HAWKINS, JR., CHAIRMAN
U.S. ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS

HEARING ON INFRASTRUCTURE PROBLEMS AND INTERGOVERNMENTAL SOLUTIONS

SUBCOMMITTEE ON GENERAL SERVICES, FEDERALISM, AND THE DISTRICT OF COLUMBIA, COMMITTEE ON GOVERNMENTAL AFFAIRS

MAY 4, 1989
WASHINGTON, DC

I am pleased to present testimony for the Advisory Commission on Intergovernmental Relations (ACIR) on America's infrastructure problems and intergovernmental solutions. Infrastructure has been an intergovernmental responsibility since the beginning of our federal republic, and the ACIR itself has a long record of involvement in infrastructure matters. Most recently, moreover, the ACIR provided supportive administrative services to the National Council on Public Works Improvement (NCPWI) during its life, and then assumed responsibility for archiving its records and disseminating its reports after NCPWI was terminated in 1988. The ACIR also has had discussions with the American Public Works Association regarding its proposals to the Congress that the ACIR be made the focal point in the federal government for public works, precisely because the ACIR is an independent, bipartisan, intergovernmental agency. There is no focal point now.

Salient issues that frame any discussion of infrastructure today include the following: (1) the nation's infrastructure is, as NCPWI phrased it, fragile, but not in ruins; (2) substantial investment is needed to upgrade the nation's infrastructure, but public revenue is in short supply; (3) more revenue is not the only solution, or always the best solution; and (4) infrastructure improvements are needed not only to improve the nation's competitive position worldwide but also to improve the quality of life, enhance economic opportunities for all Americans, and provide a solid foundation for our children's prosperity.

Five crucial questions need to be addressed with respect to infrastructure upgrading. (1) Rather than assuming that government must always increase supply in response to demand, how can we reduce inefficient and non-economically viable demands on the nation's infrastructure (e.g., inefficient uses of water)? (2) How can we link costs more closely to benefits without sacrificing equity? (3) What is the appropriate mix of public and private sector provision and production of infrastructure? (4) How can we improve the capabilities of local governments, primarily, as well as state governments, to maintain and upgrade public and private sector infrastructure investments? (5) How can we improve the compatibility of the policies and services provided by different governments, especially those of larger jurisdictions that serve smaller jurisdictions? The answers to all five questions involve intergovernmental cooperation so that federal, state, and local governments do not work at cross purposes.

Intergovernmental coordination needs to be improved in three areas: (1) fiscal policy, (2) regulatory policy, and (3) communications and planning. Coordination has taken on heightened importance because of two recent trends: (1) state and local governments have been assuming more public-works responsibilities and (2) the privatization of public works has been increasing.

Fiscal Policy

Federal aid to state and local governments for public works has declined in recent years while state and local own-source spending has increased. Overall public-works spending has risen, but new capital investment--the traditional emphasis of federal aid--has slipped, as have major maintenance and rebuilding of existing structures. Given that states have only partly replaced lost federal-aid revenues, local governments are bearing a greater infrastructure burden.

Several issues need to be addressed in any reform of federal fiscal policies. For one, federal aid sometimes stimulates unnecessary demand for infrastructure services and sometimes constrains state and local governments to provide services that are less than optimal or efficient. At the same time, there is insufficient aid for basic research, development, and demonstration projects.

Federal tax incentives for private public-works investment have been reduced dramatically, thus making it more difficult for state and local governments to create public-private partnerships. In addition, state and local infrastructure financing is being based increasingly on user fees, which are not deductible from federal income-tax liabilities. Indeed, sales taxes also are no longer deductible; yet, they are an important source of dedicated funds for local transit systems. A related issue is the non-deductibility of the fees paid to the growing number of residential community associations that maintain streets and other infrastructure services normally provided by local governments. (Shortly, the ACIR will issue a report on these "private governments.") Furthermore, given that tax-exempt bonds are very important in infrastructure financing, the 1986 limits on such bonds should be watched closely and loosened if they prove to be too restrictive.

With respect to state and local fiscal capacities, scarce federal dollars can be better targeted to areas of greatest need and of least own-source fiscal capacity. The ACIR's measures of state fiscal capacity and its current work on measures of state spending needs provide tools for improving federal-aid targeting.

Regulatory Policy

A variety of regulatory issues need to be addressed, beginning with the largely unsystematic and de facto devolutions of federal responsibilities that have been occurring since the late 1970s. In addition, federal funds that are available for public works are often subject to considerable uncertainties that make it difficult for state and local governments to plan and spend effectively. In some cases, such as highways, moreover, so-called demonstration programs are little more than pork-barrel projects. For these and other reasons, the ACIR has endorsed the devolution of selected federal-aid programs and revenue bases, and has suggested ways to do so.

Unfunded federal mandates and regulatory complexity also make it difficult for states and localities to manage infrastructure problems. The "fiscal notes" process in the Congress and Executive Order 12612 do not appear adequate in their present forms to resolve the problems arising from unilateral federal actions.

Attention must be given as well to legislative and bureaucratic fragmentation within state governments and the federal government. More and more, local governments have been able to overcome jurisdictional fragmentation in order to resolve infrastructure problems, only to confront fragmentation and delays in the state and federal arenas. In other words, state and federal "rules of the game" are no less important, and sometimes more important, than state and federal aid in helping or allowing local governments to solve problems.

Similarly, the federal government must be attentive to regulations that may quash state and local efforts to reduce infrastructure demands. For example, Minneapolis recently passed an ordinance banning nonrecyclable plastic at food stores and restaurants so as to reduce demand on the city's solid-waste disposal facilities and enhance environmental protection. Industry representatives plan to challenge the ordinance in federal court as an unconstitutional restraint on interstate commerce. The ACIR has taken no position on this or similar ordinances, but the case does illustrate a looming problem, namely, overinterpretation of federal powers under the commerce clause, which may increasingly frustrate state and local efforts to resolve the demand side of infrastructure problems. This obstacle is likely to extend to innovative pricing mechanisms as well.

Communications and Planning

The changing federal role in public works, uncertainty in federal funding, regulatory complexity, legislative and bureaucratic fragmentation, and federal court interventions have all made it difficult for governments in the federal system to communicate and plan effectively for infrastructure development. Hence, the federal government must carve out for itself a role that is reasonably stable, predictable, and supportive of state and local initiatives. Given the fiscal constraints facing all governments in the federal system as well as the novel infrastructure problems we face today, it makes sense to encourage diversity and experimentation. Furthermore, given the expertise increasingly available to states and localities, a facilitative role and, where necessary, compensatory role, seems appropriate for the federal government.

Although, for this hearing, I have focused my comments on problems and issues in the federal government's infrastructure role, state and local governments also need to address problems in their own policies and practices.

I thank you for the opportunity to present this testimony. I have only scratched the surface of infrastructure issues in the federal system; however, the ACIR remains prepared to provide continuing assistance to the Congress on these important issues.

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State Highway Funding Sources

State	Fed. Aid	M/F Taxes	Veh. Regis.	Misc. Truck Fees	Drivers Lic.	Bonds	Gen. Fund	Misc.
AL	47.4%	25.8%	8.0%	—%	—%	8.7%	—%	7.4%
AK	60.0	—	—	—	—	—	40.0	—
AZ	23.1	34.6	8.7	10.8	0.7	6.9	1.4	13.8
AR	28.9	46.9	14.3	4.1	1.2	—	—	4.6
CA	46.0	23.0	—	—	—	—	—	31.0
CO	35.7	49.1	5.2	5.1	0.8	—	—	4.1
CT	37.8	22.2	9.4	—	1.4	22.8	—	6.4
DE	35.5	21.7	—	2.4	—	—	40.4	—
DC	38.0	16.0	8.0	—	1.0	23.0	14.0	—
FL	38.0	—	18.0	—	—	—	—	44.0
GA	28.6	29.7	—	—	—	16.3	1.5	23.9
HI	38.0	33.1	5.7	0.4	—	—	—	22.8
ID	40.6	33.8	13.0	8.4	0.8	—	—	3.4
IL	24.6	34.4	27.0	—	1.6	4.0	4.3	4.1
IN	28.0	53.0	13.0*	—	—	—	4.0	2.0
IA	26.1	33.7	24.7	—	1.2	—	—	14.3
KS	41.0	27.0	19.8	1.0	1.0	—	5.6	4.6
KY	21.5	32.5	5.0	0.3	0.5	14.9	—	25.3
LA	31.0	20.0	—	—	—	43.0	6.0	0.0
ME	25.6	37.0	16.2	—	1.4	4.8	5.0	10.0
MD	25.0	27.0	8.0	1.0	—	—	—	39.0
MA	12.7	51.8	26.9*	—	—	—	0.1	8.5
MI	23.0	45.5	24.5	1.0	0.5	—	—	5.5
MN	30.8	33.4	20.7	—	1.3	—	—	13.8
MS	47.0	35.0	—	—	—	—	—	18.0
MO	27.5	36.6	20.3	0.4	1.2	—	—	14.0
MT	40.6	41.0	—	9.8	—	—	—	8.6
NE	29.7	42.0	12.0	—	—	—	—	16.3
NV	28.0	34.0	9.1	10.2	1.2	14.8	—	2.7
NH	33.0	41.7	22.3*	—	—	—	—	3.0
NJ	44.4	10.8	—	—	—	9.6	35.2	—
NM	30.2	34.9	9.0	11.5	1.0	—	—	13.4
NY	30.0	—	—	—	—	10.0	60.0	—
NC	23.2	52.5	16.6	—	3.2	—	—	4.5
ND	44.0	34.8	15.1	1.7	1.3	—	—	3.1
OH++	46.5	32.7	0.1	—	—	—	—	20.7
OK	45.9	48.8	0.2	—	—	—	2.3	2.8
OR	20.0	27.0	10.0	20.0	2.0	12.0	—	9.0
PA	**30.6**	**25.4**	**12.3**	**0.6**	**1.8**	**2.6**	**—**	**26.7**
RI	51.0	—	—	—	—	13.0	36.0	—
SC	32.2	52.2	9.2	0.1	1.1	—	0.2	5.0
SD	44.6	36.4	2.2	—	—	—	—	16.8
TN	35.6	37.6	16.2	—	—	7.0	—	3.6
TX	31.7	37.9	21.7	—	—	—	—	8.7
UT	41.5	46.6	6.4	2.3	1.6	—	0.3	1.3
VT	35.2	25.0	18.9	—	—	—	—	20.9
VA	19.9	35.1	5.8	2.0	—	—	—	37.2
WA	35.1	42.8	15.8	—	—	3.2	—	3.1
WV	41.3	30.4	9.4	—	0.5	—	—	18.4
WI	21.5	46.9	17.0	—	1.5	4.2	—	8.9
WY	36.4	12.4	14.7	—	—	—	2.1	34.4

*— Includes vehicle registrations and drivers' licenses

++ = 1987 data (1988 data unavailable)

SOURCE: TRIP-THE ROAD INFORMATION PROGRAM

TAX EXEMPT PROCEEDS FUND, INC.

PROSPECTUS
January 27, 1989

MANAGER

Reich & Tang L.P.
100 Park Avenue
New York, NY 10017

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TAX EXEMPT PROCEEDS FUND, INC.

100 Park Avenue
New York, New York 10017
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PROSPECTUS

January 27, 1989

Tax Exempt Proceeds Fund, Inc. (the "Fund") is a diversified, short-term, tax exempt money market fund that seeks to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and maintenance of liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" for Federal income tax purposes and, therefore, shareholders of the Fund that are tax exempt bond issuers, in the opinion of counsel, are expected to be exempt from the arbitrage rebate provisions of the Internal Revenue Code of 1986, as amended (the "Code"). The Fund seeks to achieve its objectives by investing primarily in a liquid money market portfolio of short-term, high quality, tax exempt fixed rate and variable rate obligations issued by state and municipal governments and by public authorities, and in participation interests therein issued by banks, insurance companies or other financial institutions that meet this Federal income tax definition. There can be no assurance that the Fund's objectives will be achieved.

The shares of the Fund will be offered primarily to entities that are issuers of tax exempt state and local bonds, such as states and municipalities and their authorities, agencies, instrumentalities and subdivisions ("Qualified Investors".)

This Prospectus sets forth concisely the information about the Fund that prospective investors will find helpful in making their investment decisions. This Prospectus should be read and retained by investors for future reference. A Statement of Additional Information dated the same date as this Prospectus containing additional information about the Fund has been filed with the Securities and Exchange Commission and is incorporated by reference into this Prospectus in its entirety. Additional copies of this Prospectus and copies of the Statement of Additional Information may be obtained on request and without charge from the Fund directly.

Reich & Tang L.P. acts as manager of the Fund and distributor of the Fund's shares. Reich & Tang L.P. is a registered investment adviser and a registered broker-dealer and member of the National Association of Securities Dealers, Inc.

The Fund intends to maintain a constant net asset value of $1.00 per share although there can be no assurance that this value will be maintained.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

INTRODUCTION

Tax Exempt Proceeds Fund, Inc. (the "Fund") is a diversified, open-end management investment company that seeks to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" for Federal income tax purposes and, therefore, Fund shareholders that are tax exempt bond issuers are expected to be exempt from the arbitrage rebate provisions of the Code. (See "Investment Objectives and Policies ".) The Fund seeks to achieve its objectives by investing principally (and in no event less than 98% of its assets) in short-term, high quality fixed rate and variable rate tax exempt securities issued by state or municipal governments and by public authorities that meet this Federal income tax definition and in participation certificates therein purchased from banks and other financial institutions. However, the Fund will not concentrate its investments in participation certificates. The Fund's portfolio will be invested primarily in municipal obligations, including municipal notes and industrial revenue bonds (issued before August 8, 1986). The Fund's investments may also include when-issued securities. The Fund will not invest in securities the interest income on which may be subject to the individual alternative minimum tax. The Fund seeks to maintain an investment portfolio with a dollar-weighted average maturity of 120 days or less, and to value its investment portfolio at amortized cost and maintain a net asset value of $1.00 per share. This is a summary of the Fund's fundamental investment policies which are set forth in full under "Investment Objectives and Policies" in this Prospectus and in the Statement of Additional Information and may not be changed without the approval of a majority of the Fund's outstanding shares; except that the Fund's fundamental investment policies of investing in securities that would qualify an investment in the Fund as a "tax exempt bond" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax may only be changed with the approval of 90% of the Fund's outstanding shares.

There can be no assurance that the Fund's objectives will be achieved. Investment by the Fund in other than "tax exempt bonds" will subject the Fund's shareholders that are tax exempt bond issuers to the arbitrage rebate provisions of the Code. However, the Fund's fundamental investment policies prohibit the Fund from investing in other than "tax exempt bonds".

The Fund's investment manager is Reich & Tang L.P. (See "Management of the Fund".) The Fund's shares are distributed through Reich & Tang L.P., with whom the Fund has entered into a Distribution Agreement pursuant to the Fund's plan adopted under Rule 12b-1 under the Investment Company Act of 1940, as amended (the "Act"). (See "Distribution Plan".)

The shares of the Fund will be offered primarily to entities that are issuers of tax exempt state and local bonds, such as states and municipalities and their authorities, agencies, instrumentalities and subdivisions ("Qualified Investors").

The Fund's investment policies were developed for the particular Federal income tax needs of Qualified Investors. Investors that are not issuers of state and local bonds and that desire to invest in a tax exempt money market fund may consider an investment in the other tax exempt money market funds managed by Reich & Tang L.P.

On any day on which the New York Stock Exchange, Inc. is open for trading ("Fund Business Day"), investors may, without charge by the Fund, initiate purchases and redemptions of shares of the Fund's common stock at their net asset value, which will be determined daily. (See "How to Purchase and Redeem Shares" page 7 and "Net

TABLE OF FEES AND EXPENSES

Annual Fund Operating Expenses

(as a percentage of average net assets)

Management Fees	0.40%
Other Expenses – After Reimbursement of Expenses	-0-
Total Fund Operating Expenses	0.40%

Example	1 year	3 years
You would pay the following expenses on a $1,000 investment, assuming 5% annual return (cumulative through the end of each year):	$ 4	$ 13

The purpose of the above fee table is to assist an investor in understanding the various costs and expenses that an investor in the Fund will bear directly or indirectly. For a further discussion of these fees see "Management of the Fund" and "Distribution Plan" herein. The Manager has agreed to bear or reimburse all the expenses of the Fund (other than the Management Fee); absent such reimbursement, Other Expenses would have been .26% based upon estimated expenses for the first fiscal year. However, the terms of the Management Contract provide that all such expenses must be borne by the Manager. The figures reflected in this example should not be considered as a representation of past or future expenses. Absent the Manager's obligation to bear the Fund's expenses, actual expenses may be greater or lesser than those shown above.

Asset Value", page 13.) Dividends from accumulated net income are declared by the Fund on each Fund Business Day. The Fund pays interest dividends monthly on the last day of each month or, if the last day of each month is not a Fund Business Day, on the preceding Fund Business Day. Net capital gains, if any, will be distributed annually, within 45 days after the end of the Fund's fiscal year. All dividends and distributions of capital gains are automatically invested in additional shares of the Fund unless a shareholder has elected by written notice to the Fund to receive either of such distributions in cash. (See "Dividends and Distributions", page 7.)

INVESTMENT OBJECTIVES AND POLICIES

The Fund is a diversified, open-end, investment company whose investment objectives are to provide its investors with high current interest income exempt from Federal income taxes, preservation of capital and liquidity. The Fund will only invest in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" as defined in Section 150(a)(6) of the Code and amplified by IRS Notice 87-22 and, therefore, shareholders of the Fund that are tax exempt bond issuers are expected to be exempt from the arbitrage rebate provisions of the Code. There can be, of course, no assurance that the Fund will achieve its investment objectives.

The Fund's assets will be invested principally (and in no event less than 98%) in short-term, high quality, fixed rate and variable rate tax exempt securities issued by or on behalf of states and municipal governments, and their authorities, agencies, instrumentalities and political subdivisions that meet this Federal income tax definition ("Municipal Obligations") and in participation certificates in such obligations purchased from banks, insurance companies or other financial institutions. The Fund will not invest in Municipal Obligations or any other securities the interest income on which may be subject to the individual alternative minimum tax. The Fund seeks to maintain an investment portfolio with a dollar-weighted average maturity of 120 days or less, and to value its investment portfolio at amortized cost and maintain a net asset value of $1.00 per share. The Fund may hold uninvested cash reserves pending investment. The Fund's investments may include "when-issued" Municipal Obligations and stand-by commitments (however, the Fund expects to invest less than 5% of its assets in such). The Fund expects to invest in participation certificates purchased from banks in industrial revenue bonds and other Municipal Obligations. The Fund will not invest in IRBs issued after August 7, 1986 the interest income from which may be subject to the individual alternative minimum tax. In view of this investment in bank participation certificates in Municipal Obligations, an investment in the Fund should be made with an understanding of the characteristics of the banking industry and the risks which such an investment may entail. See "Variable Rate Demand Instruments and Participation Certificates" in the Statement of Additional Information. The investment objectives of the Fund described in this paragraph may not be changed unless approved by a majority of the holders of the outstanding shares of the Fund that would be affected by such a change; except that the Fund's fundamental policies of investing in securities that would qualify an investment in the Fund as an investment in "tax exempt bonds" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax, may only be changed with the approval of 90% of the Fund's outstanding shares.

In view of the investment of the Fund in IRBs (issued before August 8, 1986) and participation interests therein secured by letters of credit or guarantees of banks, an investment in Fund shares should be made with an understanding of the characteristics of the banking industry and the risks which such an investment may entail. Banks are subject to extensive governmental regulations which may limit both the amounts and types of loans and other financial commitments which may be made and interest rates and fees which may be charged. The profitability of this industry is largely dependent upon the availability and cost of capital funds for the purpose of financing lending operations under prevailing money market conditions. Also, general economic conditions play an important part in the operations of this industry and exposure to credit losses arising from possible financial difficulties of borrowers might affect a bank's ability to meet its obligations under a letter of credit.

The Fund has adopted the following fundamental investment restrictions which may not be changed unless approved by a majority of the outstanding shares of the Fund. The Fund is subject to further investment restrictions that are set forth in the Statement of Additional Information. The Fund may not:

1. Borrow Money. This restriction shall not apply to borrowings from banks for temporary or emergency (not leveraging) purposes, including the meeting of redemption requests that might otherwise require the untimely disposition of securities, in an amount up to 15% of the value of the Fund's total assets (including the amount borrowed) valued at market less liabilities (not including the amount borrowed) at the time the borrowing was made. While borrowings exceed 5% of the value of the Fund's total assets, the Fund will not make any investments. Interest paid on borrowings will reduce net income.

2. Pledge, hypothecate, mortgage or otherwise encumber its assets, except in an amount up to 15% of the value of its total assets and only to secure borrowings for temporary or emergency purposes.

3. Purchase securities subject to restrictions on

disposition under the Securities Act of 1933 ("restricted securities"), except the Fund may purchase variable rate demand instruments which contain a demand feature. The Fund will not invest more than 10% of the Fund's total net assets in securities that are not readily marketable (including participation certificates and variable rate demand instruments with a right to demand payment on more than 7 days notice).

4. Invest more than 25% of its assets in the securities of "issuers" in any single industry, provided that the Fund may invest more than 25% of its assets in bank participation certificates. With respect to 75% of the total amortized cost value of the Fund's assets, not more than 5% of the Fund's assets may be invested in securities that are subject to underlying puts from the same institution, and no single bank shall issue its letter of credit and no single financial institution shall issue a credit enhancement covering more than 5% of the total assets of the Fund. However, if the puts are [illegible] by the Fund in the event of default of [illegible] of principal and interest on the underlying security, then the Fund may invest up to [illegible]% of its assets in securities underlying puts issued or guaranteed by the same institution; additionally, a single bank can issue its letter of credit or a single financial institution can issue a credit enhancement covering up to 10% of the Fund's assets, where the puts offer the Fund such default protection.

5. Invest in securities of other investment companies.

The Fund's Board of Directors has determined that the term "high quality" currently means Municipal Obligations that at the time of purchase are rated at least either "AAA" or "AA" by Standard & Poor's Corporation ("Standard & Poor's") or "Aaa" or "Aa" by Moody's Investors Service, Inc. ("Moody's") in the case of bonds; "SP-1" by Standard & Poor's or "MIG-1" or "MIG-2" by Moody's in the case of notes; "A-1" or "A-2" by Standard & Poor's or "Prime-1" by Moody's in the case of tax exempt commercial paper; "SP-1/AA" by Standard & Poor's or "VMIG-1" or "VMIG-2" by Moody's in the case of variable and floating rate demand notes, or which are unrated but are determined to be of minimal credit risk and of comparable quality by the Fund's Board of Directors on the basis of its credit evaluation of the issue, which may include an evaluation of a letter of credit, guarantee, insurance or other credit facility issued in support of the Municipal Obligations or participation certificates. (See "Variable Rate Demand Instruments and Participation Certificates" in the Statement of Additional Information.) Such instruments may produce a lower yield than would be available from less highly rated instruments. If a substantial portion of the Fund's assets are invested in such unrated demand notes, the inability of the issuers to pay such notes on demand could adversely affect the Fund's liquidity.

All investments by the Fund will mature or will be deemed to mature within one year from the date of acquisition and the average maturity of the Fund's portfolio (on a dollar-weighted basis) will be 120 days or less.

For purposes of determining whether a variable rate demand instrument held by the Fund matures within one year from the date of its acquisition, the maturity of the instrument will be deemed to be the longer of (1) the period required before the Fund is entitled to receive payment of the principal amount of the instrument through demand or (2) the period remaining until the instrument's next interest rate adjustment. The maturity of a variable rate demand instrument will be determined in the same manner for purposes of computing the

Fund's dollar-weighted average portfolio maturity.

It is anticipated that Qualified Investors will utilize the Fund for short-term investment purposes. While this may result in a high rate of portfolio turnover with increased transaction costs, it will not affect the Fund's expense ratio because of the Manager's obligation to pay all expenses of the Fund (other than the management fee).

MANAGEMENT OF THE FUND

The Fund's Board of Directors, which is responsible for the overall management and supervision of the Fund, has employed Reich & Tang L.P. (the "Manager") to serve as investment manager of the Fund. The Manager provides persons satisfactory to the Fund's Board of Directors to serve as officers of the Fund. Such officers, as well as certain other employees and directors of the Fund, may be directors or officers of Reich & Tang, Inc., the sole general partner of the Manager or employees of the Manager or its affiliates. Due to the services performed by the Manager, the Fund currently has no employees and its officers are not required to devote full-time to the affairs of the Fund. The Statement of Additional Information contains general background information regarding each director and principal officer of the Fund.

The Manager is a Delaware limited partnership with its principal office at 100 Park Avenue, New York, New York 10017. The Manager was at December 31, 1988 manager, advisor or supervisor with respect to assets aggregating in excess of $8 billion. Messrs. Oscar L. Tang, Joseph H. Reich and Robert F. Hoerle, who are officers, directors and shareholders of Reich & Tang, Inc., the sole general partner of the Manager, may each be deemed a "controlling person" of the Manager. The Manager acts as manager or administrator of fourteen other investment companies and also advises pension trusts, profit-sharing trusts and endowments.

Pursuant to the Management Contract, the Manager manages the Fund's portfolio of securities and makes decisions with respect to the purchase and sale of investments, subject to the general control of the Board of Directors of the Fund.

The Manager also performs clerical, accounting and office service functions for the Fund and provides the Fund with personnel to perform accounting and related services, calculate net asset value and yield, prepare reports to and filings with regulatory authorities, and perform such other services as the Fund may from time to time request of the Manager. The personnel rendering such services may be employees of the Manager or its affiliates.

For its services under the Management Contract, the Manager receives from the Fund a fee equal to .40 of 1% per annum of the Fund's average daily net assets up to $250 million; .35 of 1% per annum of the average daily net assets between $250 million and $500 million; and .30 of 1% per annum of the average daily net assets over $500 million for managing the Fund's investment portfolio and performing related administrative and clerical services. The Management Contract also provides that the Manager will bear the cost of, or reimburse the Fund for, all other expenses of the Fund. Therefore, the fee payable under the Management Contract will be the only expense of the Fund. The fees are accrued daily and paid monthly. Any portion of the total fees received by the Manager may be used by the Manager to provide shareholder and administrative services and for distribution of Fund shares. (See "Distribution Plan", page 11.)

DESCRIPTION OF COMMON STOCK

The Fund was incorporated in Maryland on

November 16, 1988. The authorized capital stock of the Fund consists of twenty billion shares of common stock having a par value of one-tenth of one cent ($.001) per share. Each share when issued has equal dividend, distribution and liquidation rights and each unanimous share has rights in proportion to the percentage it represents of a whole share. There are no conversion or preemptive rights in connection with any shares of the Fund. All shares when issued in accordance with the terms of the offering will be fully paid and non-assessable. Shares of the Fund are redeemable at net asset value, at the option of the shareholders. On January 5, 1989 the Manager purchased 100,000 shares of the Fund at an initial subscription price of $1.00 per share.

The shares of the Fund have non-cumulative voting rights, which means that the holders of more than 50% of the shares outstanding voting for the election of directors can elect 100% of the directors if the holders choose to do so, and, in that event, the holders of the remaining shares will not be able to elect any person or persons to the Board of Directors.

The Fund's By-Laws provide the holders of one-third of the outstanding shares of the Fund present at a meeting in person or by proxy will constitute a quorum for the transaction of business at all meetings, except that the Articles of Incorporation provide that a meeting to consider an amendment to the Fund's fundamental investment policies of investing in securities that would qualify an investment in the Fund as a "tax exempt bond" and of not investing in securities the interest income on which may be subject to the individual alternative minimum tax, 90% of the outstanding shares of the Fund must be present in person or by proxy to constitute a quorum for this particular purpose.

DIVIDENDS AND DISTRIBUTIONS

The Fund declares dividends equal to all its net investment income (excluding capital gains and losses, if any, and amortization of market discount) on each Fund Business Day and pays dividends on the last day of each month or, if the last day is not a Fund Business Day, on the preceding Fund Business Day. There is no fixed dividend rate. In computing these dividends, interest earned and expenses are accrued daily.

Net realized capital gains, if any, are distributed annually within 45 days after the end of the Fund's fiscal year.

All dividends and distributions of capital gains are automatically invested in additional Fund shares immediately upon payment thereof unless a shareholder has elected by written notice to the Fund to receive either of such distributions in cash.

HOW TO PURCHASE AND REDEEM SHARES

The Fund sells and redeems its shares on a continuing basis at net asset value and does not impose a sales charge for either sales or redemptions. All transactions in Fund shares are effected through the Fund's transfer agent which accepts orders for purchases and redemptions. There is no minimum initial investment, nor is there a minimum subsequent investment.

In order to maximize earnings on its portfolio, the Fund normally has its assets as fully invested as is practicable. Many securities in which the Fund invests require immediate settlement in funds of Federal Reserve member banks on deposit at a Federal Reserve bank (commonly known as "Federal Funds"). Accordingly, the Fund does not accept a subscription or invest an investor's payment in portfolio securities until the payment is converted into Federal Funds.

Shares will be purchased as of the first determination of the Fund's net asset value per share made after acceptance of the investor's subscription.

The Fund reserves the right to reject any subscription for its shares.

Shares are issued as of 12 noon, New York City time, on any Fund Business Day on which an order for the shares and accompanying Federal Funds are received by the Fund's transfer agent before 12 noon. Orders accompanied by Federal Funds and received after 12 noon on a Fund Business Day will not result in share issuance until the following Fund Business Day. In the case of Qualified Investors, orders received by the Fund's transfer agent before 12 noon, New York City time, on a Fund Business Day, without accompanying Federal Funds will result in the issuance of shares on that day provided that the Federal Funds required in connection with the orders are received by the Fund's transfer agent before 4:00 P.M., New York City time, on that day. Orders for which Federal Funds are received after 4:00 P.M., New York City time, will not result in share issuance until the following Fund Business Day. Fund shares begin accruing income on the day on which shares are issued to an investor.

There is no redemption charge, no minimum period of investment, and no restriction on frequency of withdrawals. Proceeds of redemptions are paid in cash. If a shareholder elects to redeem all the shares of the Fund he owns, all dividends accrued to the date of redemption are paid to the shareholder in addition to the proceeds of the redemption.

The right of redemption may not be suspended, or the date of payment upon redemption postponed, for more than seven days after shares are tendered for redemption, and the right of redemption may not be suspended, except for any period during which the New York Stock Exchange, Inc. is closed (other than customary weekend and holiday closings) or during which the Securities and Exchange Commission determines that trading thereon is restricted, or for any period during which an emergency (as determined by the Securities and Exchange Commission) exists as a result of which disposal by the Fund of its securities is not reasonably practicable or as a result of which it is not reasonably practicable for the Fund fairly to determine the value of its net assets, or for such other period as the Securities and Exchange Commission may by order permit for the protection of the shareholders of the Fund.

Redemption requests received by the Fund's transfer agent before 12 noon, New York City time, on any Fund Business Day become effective at the net asset value per share determined at 12 noon that day. Shares redeemed are not entitled to participate in dividends declared on the day a redemption becomes effective. Redemption requests received after 12 noon will result in a share redemption on the following Fund Business Day.

The Fund has reserved the right to redeem the shares of any shareholder if the net asset value of all the remaining shares in the shareholder's account after a withdrawal is less than $1,000 solely because of withdrawals from the account and not because of fluctuation in the value of the account. Written notice of a proposed mandatory redemption will be given at least 30 days in advance to any shareholder whose account is to be redeemed. During the notice period a shareholder who receives such a notice may avoid mandatory redemption by purchasing sufficient additional shares to increase his total net asset value to at least $1,000.

The redemption of shares may result in the investor's receipt of more or less than he paid for his shares and, thus, in a taxable gain or loss to the investor.

Direct Purchase and Redemption Procedures

Investors who wish to invest in the Fund may obtain a current prospectus and the subscription order form necessary to open an account by telephoning Reich & Tang L.P. at the following number:

(toll free) 800-221-3079

All shareholders will receive from the Fund confirmations of each individual purchase and redemption of Fund shares and a monthly statement listing the total number of Fund shares owned as of the statement closing date, purchases and redemptions of Fund shares during the month covered by the statement and the dividends paid on Fund shares of each shareholder during the statement period (including dividends reinvested in additional Fund shares).

Initial Purchase of Shares

Mail

Investors may send a check made payable to the Fund along with a completed subscription order form to:

Tax Exempt Proceeds Fund ,Inc.
c/o Reich & Tang L.P.
100 Park Avenue - 28th Floor
New York, New York 10017

Checks are accepted subject to collection at full value. Payment by a check drawn on any member of the Federal Reserve System can normally be converted into Federal Funds within two business days after receipt of the check. Checks drawn on a non-member bank may take substantially longer to convert into Federal Funds. An investor's subscription will not be accepted until the Fund receives Federal Funds.

Bank Wire

To purchase shares of the Fund using the wire system for transmittal of money among banks, investors should first telephone the Fund to obtain a new account number. The investors should then instruct a member commercial bank to wire their money immediately to:

The Bank of New York
Funds Processing Department
For Tax Exempt Proceeds Fund, Inc.
New account of (investor's name, address and account number) ________________
Tax ID # ________________________

The investor should then promptly complete and mail the subscription order form.

Investors planning to wire funds should instruct their bank early in the day so the wire transfer can be accomplished the same day. There may be a charge by the investor's bank for transmitting the money by bank wire, and there also may be a charge for use of Federal Funds. The Fund does not charge investors in the Fund for its receipt of wire transfers. Payment in the form of a "bank wire" received prior to 12 noon, New York City time, on a Fund Business Day will be treated as a Federal Funds payment received on that day.

Subsequent Purchases of Shares

Subsequent purchases can be made by mailing a check, by personal delivery or by bank wire as indicated above. There is no minimum for subsequent purchases of shares. All payments should clearly indicate the shareholder's account number.

Provided that the information on the subscription form on file with the Fund is still applicable, a shareholder may reopen an account without filing a new subscription order form at any time during the year the shareholder's account is closed or during the following calendar year.

Redemption of Shares

A redemption is effected immediately following, and at a price determined in accordance with, the next determination of net asset value per share following acceptance by the Fund's transfer agent of the redemption order (and any supporting documentation which it may require). Normally, payment for redeemed shares is made on the same Fund Business Day after the redemption is effected, provided the redemption request is received prior to 12 noon, New York City time. However, redemption payments will not be made until 15 days after the check (including a certified or cashier's check) used to purchase the shares has been deposited by the Fund.

A shareholder's original subscription order form permits the shareholder to redeem by written request and to elect redemption by check writing. A shareholder may only change the instructions indicated on his original subscription order form by transmitting a written direction to the Fund's transfer agent. Requests to institute or change any of the additional redemption procedures will require a signature guarantee.

When a signature guarantee is called for, the shareholder should have "Signature Guaranteed" stamped under his signature and signed at a member organization of a national stock exchange or a commercial bank or trust company in New York City (or any local commercial bank or trust company having a correspondent in New York City).

Written Requests

Shareholders may make a redemption in any amount by sending a written request addressed to:

Tax Exempt Proceeds Fund, Inc.
c/o Reich & Tang L.P.
100 Park Avenue - 28th Floor
New York, New York 10017

Normally the redemption proceeds are paid by check mailed to the shareholder of record.

Checks

By making the appropriate election on their subscription form, shareholders who are United States residents may request a supply of checks which may be used to effect redemptions. The checks, which will be issued in the shareholder's name, are drawn on a special account maintained by the Fund with the Fund's transfer agent. For Qualified Investors, checks will be pre-printed with a legend certifying compliance with specific limitations for withdrawal. Checks may be drawn in any amount. When a check is presented to the Fund's transfer agent for payment, the Fund's transfer agent, as agent for the shareholder, redeems a sufficient number of full and fractional shares in the shareholder's account to cover the amount of the check. The use of a check to make a withdrawal enables a shareholder in the Fund to receive dividends on the shares to be redeemed through the Fund Business Day on which the check clears. Checks provided by the Fund may not be certified. Fund shares purchased by check may not be redeemed by check within 15 days following the date of purchase.

There is no charge to the shareholder for checks provided by the Fund. The Fund reserves the right to impose a charge or impose a different minimum check amount in the future, if the Board of Directors determines that doing so is in the best interests of the Fund and its shareholders.

Shareholders electing the checking option are subject to the procedures, rules and regulations of the Fund's transfer agent governing checking accounts. Checks drawn on a jointly owned account may, at the shareholder's election, require only one signature. The Fund's transfer agent will not honor checks which are in amounts exceeding the value of the shareholder's account at the time the check is presented for payment. Since the dollar value of the account changes daily, the total value of the account may not be determined in advance and the account may not be entirely redeemed by check. The Fund reserves the right to terminate or modify the check redemption procedure at any time.

Investors wishing to avail themselves of this method of redemption should elect it on their subscription order form.

Qualified Investors making this election, are required to complete a certified resolution or other evidence of authorization in accordance with the Fund's transfer agent's normal practices. Appropriate authorization forms will be sent by the Fund's transfer agent to shareholders who select this option. As soon as the authorization forms are filed in good order with the Fund's transfer agent, it will provide the shareholder with a supply of checks. This checking service may be terminated or modified at any time.

DISTRIBUTION PLAN

Pursuant to Rule 12b-1 under the Investment Company Act of 1940, the Securities and Exchange Commission has required that an investment company which bears any direct or indirect expense of distributing its shares must do so only in accordance with a plan permitted by the Rule. The Fund's Board of Directors has adopted a distribution plan (the "Plan") and, pursuant to the Plan, the Fund and the Manager have entered into a Distribution Agreement with the Manager as distributor of the Fund's shares. There are no fees or expenses chargeable to the Fund under the Plan. The Fund's Board of Directors has adopted the Plan in case certain expenses of the Fund are deemed to constitute indirect payment by the Fund for distribution expenses. If a payment of fees under the Management Contract by the Fund to the Manager should be deemed to be indirect financing by the Fund of the distribution of its shares, such payments are authorized by the Plan.

Under the Distribution Agreement, the Manager, for nominal consideration and as agent for the Fund, will solicit orders for the purchase of the Fund's shares, provided that any subscriptions and orders will not be binding on the Fund until accepted by the Fund as principal.

The Plan provides that the Manager may make payments from time to time from its own resources, which may include the management fee and past profits for the following purposes: to defray the costs of, and to compensate others, with whom the Manager has entered into written agreements, for performing shareholder servicing and related administrative functions on behalf of the Fund; to compensate certain organizations for providing assistance in distributing the Fund's shares; to pay the costs of printing and distributing the Fund's prospectus to prospective investors; and to defray the cost of the preparation and printing of brochures and other promotional materials, mailings to prospective shareholders, advertising, and other promotional activities, including the salaries and/or commissions of sales personnel in connection with the distribution of the Fund's shares. The Manager, in its sole discretion, will determine the amount of such payments made pursuant to the Plan, provided that such payments will not increase the amount which the Fund is required to pay to the Manager for any fiscal year under the Management Contract in effect for that year.

FEDERAL INCOME TAXES

The Fund will elect to qualify under the Internal Revenue Code of 1986, as amended (the "Code"), as a regulated investment company that distributes "exempt-interest dividends" as defined in the Code. The Fund intends to continue to qualify for regulated investment company status. The Fund's policy is to distribute as dividends each year 100% (and in no event less than 90%) of its tax exempt interest income, net of certain deductions, and its investment company taxable income (if any). If distributions are made in this manner, dividends designated as derived from the interest earned on Municipal Obligations are "exempt-interest dividends" and are not subject to regular Federal income tax. Dividends paid from taxable income, if any, and distributions of any realized short-term capital gains (whether from tax exempt or taxable obligations) are taxable to taxable shareholders as ordinary income, whether received in cash or reinvested in additional shares of the Fund. The Fund does not expect to realize long-term capital gains and thus does not contemplate distributing "capital gain dividends" or having undistributed capital gain income within the meaning of the Code. The Fund will inform shareholders of the amount and nature of its income and gains in a written notice mailed to shareholders within 60 days after the close of the Fund's taxable year. The Tax Reform Act of 1986 (P.L. 99-514), as amended by the recently enacted Technical and Miscellaneous Revenue Act of 1988 (P.L. 100-647), ("TAMRA") affects many of the Federal tax aspects of Municipal Obligations and makes many important changes to the Federal income tax system, including a reduction in marginal tax rates, the elimination of the preferential treatment for capital gains and the elimination or reduction of many exclusions and deductions. In addition to these changes, P.L. 99-514 provides a unified state volume limitation for many types of tax exempt bonds and revises current arbitrage restrictions. Further, corporations will be required to include as an item of tax preference for purposes of the alternative minimum tax a portion of the amount by which its book income or earnings (including generally, tax exempt interest) exceeds its alternative minimum taxable income (determined without this tax preference item). Certain tax exempt interest is also included in the tax base for the additional corporate minimum tax imposed by the Superfund Amendments and Reauthorization Act of 1986.

With respect to the variable rate demand instruments, including participation certificates therein, the Fund has obtained and is relying on the opinion of bond counsel at the date of issuance or in the opinion of Battle Fowler, counsel to the Fund, that it will be treated for Federal income tax purposes as the owner thereof and the interest on the underlying Municipal Obligations will be tax exempt to the Fund. Counsel has pointed out that the Internal Revenue Service has announced in Revenue Procedure 83-55 that it will not ordinarily issue advance rulings on the question of ownership of securities or participation interests therein subject to a put and could reach a conclusion different from that reached by counsel.

If an issuer of a State or local tax exempt bond invests the proceeds of the bond issue in any "tax exempt bond", the income on which is not an item of tax preference and not includible in the alternative minimum tax computation for individual taxpayers, such issuer is not subject to the rebate provisions of Code Section 148 as amended by TAMRA. The rebate provisions would require an issuer that invests the bond proceeds in "higher yielding investments" (other than in "tax exempt bonds") to rebate a portion of the income from such investments, in order for the bond income to remain tax exempt to the bondholders. A "tax exempt bond" is any bond the income on which is excluded from gross income.

Internal Revenue Service Notice 87-22 provides that State and local bond issuers are exempt from the rebate requirements even if the bond proceeds are invested in tax exempt bonds indirectly through a qualified regulated investment company, that is, a corporation (a) that (i) meets the regulated investment company requirements of Section 852(a) of the Code, (ii) has one class of authorized and outstanding stock, and (iii) to the extent practicable invests all its assets in tax exempt bonds, and (b) 98% of the income of which is attributable to, or 98% of the weighted average of the assets of which are, tax exempt bonds. Notice 87-22 may be relied on until proposed regulations are issued. To date no proposed regulations have been issued although it is expected that such regulations will be consistent with the Notice.

Since the Fund is established primarily for issuers of tax exempt bonds that do not wish to be subject to the Code's rebate requirements, the Fund intends to comply with the provisions of Notice 87-22 and will invest only in tax exempt bonds the income from which, in the opinion of bond counsel at the date of issuance or in the opinion of Battle Fowler, counsel to the Fund, is not subject to the individual alternative minimum tax provisions.

The exemption of interest income for Federal income tax purposes does not necessarily result in an exemption under the income or other tax laws of any state or local taxing authority. Shareholders of the Fund may be exempt from state and local taxes on distributions of tax exempt interest income derived from obligations of the state and/or municipalities of the state in which they may reside but may be subject to tax on income derived from obligations of other jurisdictions. Shareholders should consult their own tax advisors about the status of distributions from the Fund in their own states and localities.

GENERAL INFORMATION

The Fund was incorporated under the laws of the State of Maryland on November 18, 1988 and it is registered with the Securities and Exchange Commission as a diversified, open-end, investment company.

The Fund prepares semi-annual unaudited and annual audited reports which include a list of investment securities held by the Fund and which are sent to shareholders.

For further information with respect to the Fund and the shares offered hereby, reference is made to the Fund's registration statement filed with the Securities and Exchange Commission, including the exhibits thereto. The Registration Statement and the exhibits thereto may be examined at the Commission and copies thereof may be obtained upon payment of certain duplicating fees.

NET ASSET VALUE

The net asset value of the Fund's shares is determined as of 12 noon, New York City time, on each Fund Business Day. Fund Business Day means weekdays (Monday through Friday) except customary national business holidays and Good Friday. It is computed by dividing the value of the Fund's net assets (i.e., the value of its securities and other assets less its liabilities, including expenses payable or accrued but excluding capital stock and surplus) by the total number of shares outstanding.

The Fund's portfolio securities are valued at their amortized cost in compliance with the provisions of Rule 2a-7 under the Investment Company Act of 1940. Amortized cost valuation involves valuing an instrument at its cost and thereafter assuming a constant amortization to maturity of any discount or premium, except that if fluctuating interest rates cause the market value of the Fund's portfolio to deviate more than 1/2 of 1% from the value determined on the basis of amortized cost, the Board of Directors will consider whether any action should be initiated. Although the amortized cost method provides certainty in valuation, it may result in periods during which the value of an instrument is higher or lower than the price an investment company would receive if the instrument were sold. The Fund intends to maintain a stable net asset value at $1.00 per share although there can be no assurance that this will be achieved.

CUSTODIAN, TRANSFER AGENT AND DIVIDEND AGENT

The Bank of New York is the custodian for the Fund's cash and securities and the is the transfer agent and dividend agent for the shares of the Fund. The bank does not assist in, and is not responsible for, investment decisions involving assets of the Fund.

State of Connecticut
OFFICE OF THE TREASURER

FRANCISCO L. BORGES
TREASURER

EDWARD J. PORAND JR.
DEPUTY TREASURER

GENERAL MEMORANDUM

November 30, 1988

TO: Honorable J. William Burns
Commissioner
Department of Transportation
P.O. Drawer A
24 Wolcott Hill Road
Wethersfield, CT 06109

FROM: Francisco L. Borges, State Treasurer
J. Edward Caldwell, State Comptroller
Anthony V. Milano, Secretary, OPM

SUBJECT: Implementation of Public Act 88-258, an Act Concerning the Establishment of a Tax-Exempt Bond Proceeds Fund (TEBPF)

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20 Trinity Street Hartford, Connecticut 06106
An Equal Opportunity Employer

I. THE TAX-EXEMPT BOND PROCEEDS FUND

Public Act 88-258 authorizes the Treasurer to establish a tax-exempt mutual fund for the investment of state bond proceeds. This legislation was enacted to meet provisions of the Tax Reform Act of 1986.

Stated simply, for programs and projects which pass through the proceeds of tax-exempt bonds, the Tax Reform Act defined "expenditure" as the point at which the ultimate recipient makes a payment to a contractor or vendor. Until such "expenditure" is made, funds must be invested. The State, as the bond issuer, must track those thousands of investment streams even though it no longer has direct control of the funds, must compare the earnings back to the rate of interest on the underlying bonds, and must "rebate" excess earnings to the federal government, even if those earnings were received by others. Potential payments of a portion of such earnings would be due the federal government, even if this investment was only overnight.

The level of tracking required is simply not feasible. The Tax-Exempt Bond Proceeds Fund (TEBPF) is a permitted alternative, provided all pass-throughs of tax-exempt bond proceeds are invested therein.

Up to now, as an interim step to keep your programs in operation, the State has been fronting all pass-through projects with cash from other sources since the effective date of the Tax Reform Act of 1986. It is no longer possible to do so. Immediate start-up of the TEBPF so that bonds may again be issued for your programs is a matter of some urgency. The TEBPF must commence operations by January 1, 1989.

The purposes of this memorandum are as follows:

- To inform State agencies about the TEBPF and the urgency of its establishment
- To explain the new project identification system that all agencies will need to use for projects that are directed through the mutual fund and ultimately will be used to identify all capital projects funded from bond proceeds.
- To describe fully the operating characteristics and requirements of the TEBPF

II. BASIC TEBPF REQUIREMENTS

Payments from State tax-exempt bond proceeds, regardless of the date of approval or allotment, made for grant or loan programs of the state must be deposited into TEBPF beginning January 1, 1989.

The monies deposited may be withdrawn by the grantee/loan recipient when they are needed to meet an expenditure for a project or to refund the unexpended portion of the grant back to the state.

The following is a brief listing of questions typically asked about how this mutual fund will be set-up and what agencies must do to comply with these requirements.

- Participants: Who must participate in the tax-exempt mutual fund?

All State agencies which administer grants and certain loans financed from tax-exempt bond proceeds. These grants or loans are to municipalities, other public agencies or 501(c)(3) tax-exempt organizations.

- Tax-Exempt vs. Taxable: How does an agency know whether or not the grant-in-aid or loan is taxable or tax-exempt?

Prospectively, agencies must fill out a tax questionnaire and submit that information to OPM. OPM will tentatively classify each project as either "governmental" or "private activity" and this information will appear on the State Bond Commission agenda item. To the extent possible, entire programs will either be included in the TEBPF, or not be included.

For both projects in progress and future projects, OPM and the Treasurer's Office will work with you to determine which must be included in the fund. See Part III and Part IV, below.

- Programs administered on a reimbursement basis: What if your grant program is administered on a reimbursement basis? Does it still have to go through the mutual fund?

Yes. Programs which operate on a reimbursement basis will be included initially in order to reduce the likelihood of error.

- o Timing of payments through the TEBPF: Does it make any difference that the State Bond Commission approved the grant five years ago?

All payments made after January 1, 1989 from tax-exempt bond proceeds must go through the mutual fund, no matter when approved or allotted.

- o Payments to program recipients: How do program recipients receive and make payment?

Through the procedures outlined below, at the point in the payment sequence when a check would have gone out from the State Comptroller's Office to the recipient, a deposit will instead be made in the recipient's name in the TEBPF. The recipient will be issued checks against that account. The checks will be honored only if the "Recipient," "Project Name," and "Project No." blanks have been filled in and the appropriate one of two certifications printed on the face of the check has been properly filled out. The first certification applies to any payment for which a municipality has not already advanced its own funds. The certification indicates that the check is being issued for a payment to a contractor/vendor for the purpose for which the funds were granted. Contractor/vendor generally means any payee other than the recipient.

If the check is made payable to the recipient in the case of a reimbursement, the recipient must certify that the payment is a reimbursement and must indicate the date of payment and source of funds being reimbursed. Withdrawals from TEBPF made payable to the recipient should be audited by your agency against proof of expenditure.

Checks which are made out to a recipient, but for which the first rather than the second certification has been completed will not be honored.

- O Sequence of events that lead to payment: What will happen when a payment request is made to the Comptroller's Office for a program recipient?

    1. The State Comptroller's Office will post project funds electronically for grant recipient payments (no check required).

    2. The State Treasurer will transfer project funds via electronic funds transfer to the (TEBPF) fund manager (Reich & Tang).

3. The deposit of the project funds will be made by Reich & Tang to the recipients TEBPF account.

4. Reich & Tang will honor all requests for payments made by the program recipient to contractors or vendors upon completion of certification printed on the face of the check.

III. DEFINITION OF "PROJECT" FOR PURPOSES OF THE TEBPF AND THE OPM CAPITAL BUDGET SYSTEM

Payments under a grant or loan program made from tax-exempt bond proceeds deposited into TEBPF must have identification. Identification will be made on a project by project basis. Treasury, the Comptroller's Office and OPM will work with agencies to define the projects.

A project is defined as having:

1. The same tax classification (as determined from the tax questionnaire)
2. The same administering State agency
3. The same recipient signatory authorization

Example:

A "project": grants for rehabilitation of various housing developments (generally "governmental") to the Hartford Housing Authority (a single recipient and signatory) made by the Department of Housing (a single administering State agency).

A "project": school construction grants (generally "governmental") to the City of Hartford (a single recipient signatory) for work at Hartford Public High School and Bulkeley High School.

Not a "project": grants to the Hartford Housing Authority and the New Haven Housing Authority (different recipient signatories) by the Department of Housing for rehabilitation of various housing developments

Not a "project": grants to the Hartford Housing Authority and the City of Hartford (differing signatory authorities) for asbestos removal.

IV. PROJECT NUMBERING

The numbering system which is being established for the TEBPF will be used for all State of Connecticut bond projects once the OPM Capital Budgeting System is established. The project numbering system will be as follows:

A. Agencies must maintain the existing numbering system using the bond fund, agency, SID, and project number. A new project ID system, in addition to the existing system, should be recorded on Line 2 after the name of the payee.

B. Agencies must use the 80,000 batch series to identify for the Comptroller and Treasurer the payments to the tax-exempt mutual fund.

C. Project ID must be recorded on the TEBPF Journal and will be a 10 digit numerical sequence as follows:

   1. First four digits - the agency number
   2. The next two digits - the program code
   3. The next four digits - the project number

   Please note that within the definition of a project each project number must be unique to that particular project. This unique project number must be maintained for that project and only that project, including any supplemental funding.

D. The following instructions are intended as a guide to assist agencies in coding of capital projects and is divided into two numbering sequences as follows: 1) State grants-in-aid, advances-in-aid, and loan programs; and 2) State construction/acquisition projects.

   1. State Grants-In-Aid, Advances and Loans:

      a. An agency must use the first four digits in the ten digit project ID for the agency number. This agency code should be one unique agency number.

      b. The next two digits should be used by an agency to identify major programs. An agency should use a two digit numbering system starting with 01 through 49.

c. The next four digits must be used by an agency to identify specific projects within a program. The project numbers will be within the range from 0001 to 9999.

d. Also, lump sum requests should be coded using the program "00," and project code "0000."

Please note that these numbers are unique to a project, and must be maintained through all project phases, i.e., land acquisition, design and construction including any supplemental funding. An example of how a project ID could be developed for the Department of Housing is given in Attachment I, and an example for the Department of Education is given in Attachment II.

2. State Construction Projects:

Once the OPM Capital Budget System is implemented, agencies will be required to code all capital projects in accordance with the new ten digit project identification code. The assignment of project ID codes will be detailed in future directives.

V. PROCEDURE FOR ESTABLISHMENT OF PROJECT NUMBERING FOR ALL GRANT AND LOAN PROGRAMS

The procedure will be as follows:

A. With advice and consultation from OPM, agencies must prepare the following forms:

1. "Listing of Programs to be Funded with Tax-Exempt Bond Proceeds to be Deposited in the Tax-Exempt Bond Proceeds Fund" (Attachment III)

2. "Listing of Programs that Will Not Be Deposited in the Tax-Exempt Bond Proceeds Fund" (Attachment IV).

All of your agency's bond-funded grant and loan programs must be included on one of the two forms. The Agency Head must sign and date these forms and submit copies to OPM, Office of the Treasurer, and Office of the Comptroller, Accounting Systems Division, by December 5, 1988.

B. For all projects and programs that will be included in the Tax-Exempt Mutual Fund program, each agency should assign project numbers, list them on the "Grant/Loan Project Identification Number Assignment" form (Attachment V) and submit the forms to OPM for review. (Agencies should retain a copy for their records). The forms must be received by OPM by December 15, 1988.

C. OPM will review the forms and will contact the agency within five working days, as follows:

If approved:

OPM signs and dates the form, makes copies, and distributes as follows:

1 copy to Treasurer
1 copy to the Agency
1 copy for OPM files

If unapproved:

OPM will contact the agency by phone to resolve any problems.

Possible problems include:

- Incorrect categorization of program
- Incorrect or inconsistent definition of project (e.g. more than one grant recipient covered in single project)
- Duplicate project numbers

D. The Treasurer will not activate a TEBPF account or process payments for any project for which there has not been an approved Project Number.

VI. ESTABLISHMENT OF PROJECT ACCOUNTS

The firm of Reich and Tang has been hired to manage the TEBPF. The fund manager will establish project accounts within TEBPF for each grant/loan recipient.

Reich and Tang, using the approved listing established in accordance with Part V, will work with project recipients to set up their accounts. A new account letter used to establish withdrawal authorization will be completed and signed by project recipients. A new account letter must be completed for each project by the grant/loan recipient. The grantee agency must provide a new account letter to the recipient for completion. The recipient will transmit this new account letter to Reich and Tang.

VII. PAYMENT PROCEDURE

A. IDENTIFICATION

1. TEBPF payments must be processed in separate expenditure batches.

2. The batch number must begin with the 80,000 series and be initialized each fiscal year. Payee information on the batch, CO-19, should read:

   "TAX-EXEMPT BOND PROCEEDS FUND WIRE DEPOSIT - NO CHECK REQUIRED"

   The amount should be the total for all payees listed. Listing of individual payees on the CO-19 is not required. The batch should be stamped in the upper right hand corner - "TEBPF"

3. A TEBPF Journal (Attachment VI) is to be completed. This journal provides information as to deposit project account numbers and amounts. The attached sample may be copied for use until a supply of printed forms is available.

4. Payee information on the CO-17 or CO-17L should appear as follows:

   NAME - line 1: Town of __________, if a town, or payee name
   line 2: ACCT. # XXXX-XX-XXXX (agency number-program number-project number, i.e. the project identifier code)

   ADDRESS - MUST be left blank

   Complete all other payee information as required in the Expenditure Section of the State Accounting Manual (SAM).

B. TRANSMITTAL

1. To the Comptroller - Special payment batches, for TEBPF (Attachment VII), numbered in the 80,000 series, will be sent to the Central Accounts Payable Division (CAP) of the Comptroller's Office

for payment processing.

2. To the Treasurer - AT the same time as a payment batch is forwarded to CAP, the Treasurer's copy of the TEBPF journal will be sent to:

   The Office of the State Treasurer
   20 Trinity Street
   Hartford, CT

   ATT: TEBPF Coordinator

C. CORRECTIONS AND ADJUSTMENTS

1. Improperly identified accounts -

   Payment made for deposit into TEBPF that are not properly identified or do not have an account set up with the fund manager will require corrective action by the agency originating the claim. Telephone contact will be made by the TEBPF manager concerning improperly identified payments.

   Subsequently, a TEBPF journal noting correction and the date of the correction should be forwarded to Treasury. An area has been provided for corrections on the TEBPF journal.

   In the event that a State payment is deposited into TEBPF in error, and the agency is notified by Reich & Tang that an account does not exist for the project, the following procedure should be followed:

   a)Reich and Tang will deposit unidentified payments into a State account awaiting advice of disposition from the agency.

   b) The agency should request a refund of expenditure by wire deposit from the TEBPF by:

      1. Completing a TEBPF correction journal indicating that a deposit was made to TEBPF in error. An explanation must be given for the reason the payment was made to the TEBPF. Certification by the agency is required on all corrections made to TEBPF deposits. The batch number on the TEBPF correction journal should be the original batch number, a dash and a sequential number

beginning with 1 for the first adjustment on a batch (example Batch 80,005-1).

2. Filling out a deposit slip, CO-39, following procedures prescribed in the SAM Coding Section, paragraph 2.2.3, Refunds of Expenditures - other than Budgeted Appropriations.

3. Submitting both documents, the TEBPF correction journal and the CO-39, to Treasury, TEBPF Coordinator.

4. Upon completion of the wire deposit, a receipted CO-39 will be returned to the agency as advice of refund of the TEBPF deposit error.

2. Misdirected payments -

Agency
[illegible]
Form CO790
+
then prepares
new payment list
in 80,000 series

If the agency fails to properly identify the payment batch as a tax-exempt mutual fund payment and a check is mailed to the recipient in error, the recipient must return the undeposited check to the agency. The agency must then follow procedures as prescribed in the State Accounting Manual, Expenditure Section, Vendor Check Cancellation Procedure.

3. Improperly deposited payments -

a. Money deposited to an incorrect project number - an adjustment can be made on the TEBPF journal, within the correction area. Both the correct and incorrect information must be reported. The incorrect amount should be enclosed in parenthesis. See section C-1 for an explanation of batch numbering.

b. Money deposited incorrectly to TEBPF - effect recovery from the recipient by check made payable to the State. Follow the procedures as prescribed in SAM for refund of expenditures.

c. Deposit amount incorrect:

i Amount greater than - effect recovery from payee directly using the already-established procedures for refund of expenditures

ii Amount less than - issue an additional payment for the difference (on an 80,000 batch)

iii Amount differs between projects - follow the rules established in (c)-i and (c)-ii above.

D. RECONCILIATION

It is recommended that expenditures paid to grantees and loan recipients for deposit into TEBPF be reconciled with the periodic statements provided by the TEBPF fund manager. Boxes 7 & 8 and the blank column between boxes 12 & 13 of the TEBPF journal have been included to allow for reconciliation.

Errors discovered during reconciliation should be reported to the Treasurer utilizing the TEBPF journal in the area provided for corrections.

VIII. NONCOMPLIANCE WITH TEBPF REQUIREMENTS

If through an error, a recipient receives funds directly and fails to comply with the state's deposit requirement for tax-exempt bond fund grant-in-aid program monies, the recipient will be in violation of State law and all State grant/loan awards may be in jeopardy.

The continued tax-exempt status of all State of Connecticut bond issuance depends upon the successful implementation of the TEBPF. If a pattern develops in which a State agency has not done what is required to assure that all of its payments to grant and loan recipients from tax-exempt bond proceeds flow through the TEBPF, all such payments by that agency may be halted until correction is made.

IX. MODIFICATION OF GRANT AND LOAN CONTRACTS

In order to assure that the fund will operate in a way which permits the bond counsel to approve the issue of bonds as tax-exempt, a modification to new grant and loan contracts paid with tax-exempt bond proceeds will need to be implemented.

Guidelines will be issued at a later date to clarify this issue. However, please keep in mind that new tax-exempt bond fund grant-in-aid program contracts must require that:

A. Qualifying grant and loan money be invested in TEBPF.

B. The proceeds from the bonds only be withdrawn from a TEBPF account for a contractor or vendor payment and not be reinvested after release from TEBPF, unless the payment is a reimbursement. If a reimbursement, proof of expenditure (generally a cancelled check) must be provided to the State Agency.

C. Fund withdrawal requests be accompanied by a signed certification that the moneys will be used immediately for project expenditure.

D. Unexpended funds be returned to the State.

X. GENERAL

Best efforts have been made to define the procedures that will fit in all cases. However, there may be exceptions to be dealt with and your cooperation and forbearance will be necessary in the start up process.

Questions may be directed as follows:

PROJECT CLASSIFICATION OR BOND COUNSEL ISSUES:

Office of the State Treasurer, TEBPF Coordinator - 566-5054
Office of Policy and Management, Capital Program Unit
566-4757

PAYMENT PROCEDURE:

Office of the State Comptroller, Central Accounts Payable,
Special Handling Section - 566-3895

TEBPF ACCOUNT INFORMATION:

Fund Manager, Reich & Tang - 1-800-221-3079

ATTACHMENT I
DEPARTMENT OF HOUSING

Step 1

Determine the agency number 1150

Step 2

List the major grant/advance/loan programs and assign a unique program code for all bond financed programs starting with code 01 as follows:

	Program Description	Agency - Code
1)	Grants for innovative housing for the homeless	1155 - 01
2)	Grants/loans for Moderate Rental Housing Rehabilitation	1155 - 02
3)	Grants for Affordable Housing	1155 - 03
4)	Housing Purchase and Rehabilitation	1155 - 04
5)	Grants/Loans for Congregate Elderly Housing	1155 - 05
6)	Grants/Loans for Rental Housing for the Elderly	1155 - 06
7)	Grants for Community Development/ Neighborhood Rehabilitation	1155 - 07
8)	Grants/Loans for Limited Equity Cooperatives	1155 - 08
9)	Grants/Loans for Mutual Housing	1155 - 09
10)	Grants for Housing Site Development	1155 - 10
11)	Loans/Advances to Community Housing Development Corporations	1155 - 11
12)	Grants for Land Bank and Land Trust	1155 - 12
13)	Loans/Advances for Urban Homesteading	1155 - 13
14)	Energy Conservation Loan Programs	1155 - 14
15)	Grants to Public Housing Authorities for removal of Hazardous Material	1155 - 15
16)	Loans for Removal of Hazardous Materials	1155 - 16
17)	Grants-Loans to Senior Citizens for Homeowner Emergency Repairs	1155 - 17
18)	Lump sum for all housing purposes	1155 - 00

Step 3

Determine how specific projects will be coded within program categories using the number sequence 0001 through 9999. Please note that this specific project ID must not exceed 9999. It is important to make sure that the definition of a project is maintained at the proper level in order to not exceed the number 9999.

Example

A) An elderly housing grant-in-aid to New Haven
Project ID - 1155-06-0001
B) An affordable housing grant to Hartford
Project ID - 1155-03-0001

ATTACHMENT II
DEPARTMENT OF EDUCATION

Step 1

Determine the agency number - 7001

Step 2

List the major grant programs and assign a unique program code for all bond financed programs starting with code 01 as follows:

Project Description	Agency - Code
1) Grants-in-aid for local school building projects	7001 - 01
2) Grants-in-aid for vocational education equipment	7001 - 02
3) Projects for CPTV	7001 - 03

Step 3

Determine how specific projects will be coded within program categories using the number sequence 0001 through 9999. Please note that this specific project ID must not exceed 9999. It is important to make sure that the definition of a project is maintained at the proper level in order to not exceed the number 9999.

Example

A) A school building project in Hartford that is determined to be a governmental purpose in accordance with the 1986 Tax Reform Act.
Project ID - 7001-01-0641

B) A grant for vocational education equipment to Hartford that is determined to be governmental.
Project ID - 7001-02-0641

LISTING OF PROGRAMS TO BE FUNDED WITH TAX-EXEMPT BOND PROCEEDS TO BE DEPOSITED IN THE TAX-EXEMPT BOND PROCEEDS FUND IN ACCORDANCE WITH PUBLIC ACT 88-258

Agency Name: ______________ Contact Person: ______________ Phone ______________

Agency/Program No.	Program Description	Comments
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		
_ _ _ _ _ _		

______________ DATE

______________ Approved by Agency Head

Instructions: This form should be used to establish program accounts for the Tax-Exempt Bond Proceeds Fund. Please submit the original to OPM with copies to the State Treasurer and the State Comptroller. NOTE: An Agency should use only one agency number.

LISTING OF PROGRAMS THAT
WILL NOT BE DEPOSITED IN THE TAX-EXEMPT BOND PROCEEDS FUND

Agency Name: ____________ **Contact Person:** ____________ **Phone:** ____________

Agency/Program No.	Program Description	Justification for Exemption from

____
DATE

____
APPROVED BY AGENCY HEAD

INSTRUCTIONS: This form should be used to list those programs that do not need to utilize the Tax-Exempt Bond Proceeds Fund. An example would be any program whose payments derive from taxable bonds. If there is any doubt about the eligibility of a project for exemption from the Tax-Exempt Bond Proceeds Fund, it should be included in the TEBPF program. Please submit the original of this form to OPM with copies to the State Treasurer and the State Comptroller. NOTE: An Agency should use only one agency number.

GRANT/LOAN PROJECT IDENTIFICATION NUMBER ASSIGNMENT

Agency Name: ______________________ Contact Person: ______________________ Phone: ____________

Capital Project Number	Title/Name of Recipient	Statutory Reference	Bond Commission Agenda		Fund
			Date	Item #	

OPM APPROVAL:

BY: ______________________ DATE: ______________________

ATTACHMENT VI

TAX-EXEMPT BOND PROCEEDS FUND (TEBPF)
DEPOSIT JOURNAL
[illegible]

STATE OF CONNECTICUT
OFFICE OF THE STATE TREASURER

(1) BATCH DATE	(2) BATCH NUMBER	(3) AGENCY NUMBER	(4) AGENCY TELEPHONE NO.-CONTACT PERSON	(5) PAGE OF

(6) BATCH TOTAL	(7) DEPOSIT DATE (PER FUND MANAGER)	(8) TOTAL DEPOSITED (PER FUND MANAGER)

(9) AGENCY	(10) BOND FUND	(11) PAYEE / PROJECT NAME	(12) PROJECT NUMBER		(13) DEPOSIT AMOUNT	(14) EXPENDITURE PROJECT TOTAL	(15) ACT N/F
			(16) PAGE TOTAL				

CORRECTIONS

CERTIFICATION	AGENCY	TREASURY

DISTRIBUTION PART 1 - TREASURER PART 2 - AGENCY

ATTACHMENT VI

FORM NAME: Tax-Exempt Bond Proceeds Fund (TEBPF)

PURPOSE: Submitted to Treasury at the same time as the Tax-Exempt Mutual Fund Expenditure Batch is submitted to the Comptroller's Office - Central Accounts Payable.

DISTRIBUTION: Agency, Treasury, Fax copy to TEBPF Fund Manager

COMPLETION INSTRUCTIONS:

Agency must complete blocks 1-6 and 9-16. All blocks are required except #15. This form must be completed and sent to the Treasurer's Office for reconciliation with the Comptroller's Office and the Fund Manager's statement.

X-REF NUMBER	MAX LENGTH	NAME/DESCRIPTION
1		BATCH DATE - Date agency transmitted to Comptroller's Central Accounts Payable.
2	5	BATCH NUMBER - Must be 80,000 series.
3	4	AGENCY NUMBER - Submitting Agency Number - Must be the same as original Expenditure batch.
4		AGENCY TELEPHONE NUMBER/CONTACT PERSON
5		PAGE OF - Page number out of total number of pages in this listing.
6	15	BATCH TOTAL - Dollar Amount of Batch.
7		DEPOSIT DATE (PER FUND MANAGER) - To be completed when reconciling fund statement - date monies deposited.
8	15	TOTAL DEPOSITED (PER FUND MANAGER) - To be completed when reconciling fund statement - should equal batch total.
9	4	AGENCY - Expending Agency Number
10	4	BOND FUND - Tax-Exempt Bond Appropriation Fund

ATTACHMENT VI

X-REF NUMBER	MAX LENGTH	NAME/DESCRIPTION
11		PAYEE/PROJECT NAME - List 2 lines - (double space after each payee) Line 1 - Town of xxxxx Line 2 - Project Name - May be a detailed description that will identify for the grantee/loan recipient the payment being made.
12	10	PROJECT NUMBER - Must be 10-digit project number per OPM's specifications.
13	15	DEPOSIT AMOUNT - Individual payee amount.
14	15	EXPENDITURE PROJECT TOTAL - Cumulative total.
15	1	ACT N/F - Action - New Account or Final Payment.
16	15	Page Total

15575

EXPENDITURE BATCH HEADER
O-19 REV. 2/98
(Stock No. 6938-109-01)

ATTACHMENT VII

STATE OF CONNECTICUT
OFFICE OF THE STATE COMPTROLLER

TO: Central Accounts Payable Division, 30 Trinity Street, Hartford, CT 06106

(1) AGENCY NO.	(2) BATCH NUMBER	(3) NO. OF DOC.	(4) BATCH AMOUNT
1155	80,000	1	300,000.00

(5) SUBMITTED BY (Agency Name)	(6) TELEPHONE NUMBER - BUSINESS OFFICE
Dept. of Housing	x1234

(7) PAYEE	(8) PAYEE LIST ☐	(9) PURCHASE ORDER NUMBER	(10) REQ. FOR RES. OF FUNDS OR TRAV. AUTH. NO.	(11) AMOUNT OF INVOICE
TAX-EXEMPT BOND PROCEEDS FUND Deposit				300,000.00

NO
CHECK REQUIRED

(12) CHECK THE APPROPRIATE BOX ☐ TAPE ☐ ON-LINE ☒ CENTRALLY

AGENCY CERTIFICATION

As a duly authorized agent of the above named agency, I do hereby certify that to the best of my knowledge the amount shown above equals the total of the invoices and/or payrolls submitted herewith for payment and are valid claims against the State; no commission, bonus or reward has been promised or received or is expected on account thereof, by an officer or employee of the State; and the expenditures are authorized and properly chargeable to appropriations as indicated.

(13) AUTHORIZED SIGNATURE (Agency Head)	(14) CONTACT PERSON	(15) DATE

DISTRIBUTION: Original — Comptroller Part 2 — Agency

AMERICAN SILVER CITY MUSEUM
AMOS HOUSE INC
ANCIENT BURYING GROUND ASSOCIATION
ANDOVER, TOWN OF
ANSONIA HOUSING AUTHORITY
ANTIQUARIANS & LANDMARKS SOCIETY
APT FOUNDATION, THE
AREA COOPERATIVE EDUCATION SERVICE
ARTISTS COLLECTIVE INC
ASHFORD, TOWN OF
AVON, TOWN OF

BARKHAMSTED, TOWN OF
BEACON FALLS, TOWN OF
BERLIN, TOWN OF
BETHANY, TOWN OF
BETHSAIDA COMMUNITY (NORWALK)
BIBLIOMATION INC
BLOOMFIELD, TOWN OF
BOLTON, TOWN OF
BOOTH & DIMOCK MEMORIAL LIBRARY
BOYS VILLAGE YOUTH & FAMILY
BRANFORD DAY CARE
BRANFORD HOUSING AUTHORITY
BRANFORD, TOWN OF
BRIDGEPORT COMMUNITY HEALTH CENTER
BRIDGEPORT ECONOMIC DEVELOPMENT CORPORATION
BRIDGEPORT, CITY OF
BRISTOL EMERGENCY SHELTER & HOUSING COALITION
BRISTOL HOUSING SITE DEVELOPMENT AGENCY
BRISTOL, TOWN OF
BROAD PARK DEVELOPMENT CORPORATION
BROOKFIELD HOUSING AUTHORITY
BROOKFIELD, TOWN OF
BROOKLYN HOUSING AUTHORITY
BROOKLYN, TOWN OF
BUSHNELL PARK CAROUSEL SOCIETY INC

CANTERBURY, TOWN OF
CAPITAL REGION EDUCATION COUNCIL
CAPITAL REGIONAL LIBRARY COUNCIL
CENTRAL NAUGATUCK VALLEY HELP INC
CHARTER OAK TEMPLE RESTORATION ASSOC
CHEMICAL ABUSE SERVICES AGENCY
CHENEY HALL FOUNDATION INC
CHESIRE, TOWN OF
CHESTER, TOWN OF
CHILD & FAMILY AGENCY OF SOUTHEASTERN CT
CHILD GUIDANCE CENTER OF GREATER BRIDGEPORT
CHILD GUIDANCE CLINIC OF SOUTHEASTERN CT
CHILD GUIDANCE CLINIC OF WATERBURY
CHILDRENS' CENTER
CHILDRENS' HOME OF CROMWELL
CHURCH OF THE GOOD SHEPHERD

CLINTON HOUSING AUTHORITY
CLINTON, TOWN OF
COLCHESTER HOUSING AUTHORITY
COLCHESTER, TOWN OF
COLEBROOK, TOWN OF
COLUMBIA, TOWN OF
COLUMBUS HOUSE
COMMITTEE ON TRAINING AND EMPLOYMENT
COMMUNITY ACTION COMMITTEE OF DANBURY
COMMUNITY HEALTH AFFILIATES
COMMUNITY HEALTH CENTER
COMMUNITY LAND TRUST OF WINDHAM
COMMUNITY PROVIDER CONSORTIUM
COMMUNITY RENEWAL TEAM OF GREATER HARTFORD
COMPANY OF FIFERS & DRUMMERS
CONGREGATIONAL CHURCH OF THOMPSON
CONTINUUM OF CARE
COOPERATIVE EDUCATIONAL SERVICES
CORNWALL, TOWN OF
COVENTRY HISTORICAL SOCIETY INC
COVENTRY HOUSING AUTHORITY
COVENTRY, TOWN OF
CREATIVE HOUSING (HARTFORD) INC
CT ANTIQUE FIRE APPARATUS ASSOCIATION
CT CHILDREN' MUSEUM
CT ELECTRIC RAILWAY ASSOC
CT HALFWAY HOUSE
CT HISTORICAL SOCIETY
CT HOLDING ACCOUNT
CT JUNIOR REPUBLIC
CT NAUTILUS COMMITTEE
CT PUBLIC BROADCASTING
CT RENAISSANCE INC
CT RESOURCES RECOVERY AUTHORITY
CT STATE FIREMAN'S ASSOC
CT TRUST FOR HISTORIC PRESERVATION INC
CURTIS HOME INC

DANBURY HOUSING AUTHORITY
DANBURY, TOWN OF
DANIELSON, BOROUGH OF
DARIEN, TOWN OF
DEEP RIVER, TOWN OF
DERBY HOUSING AUTHORITY
DERBY, TOWN OF
DURHAM, TOWN OF

EAST CONN INC
EAST GRANBY, TOWN OF
EAST HADDAM, TOWN OF
EAST HAMPTON HOUSING AUTHORITY
EAST HAMPTON, TOWN OF
EAST HARTFORD HOUSING AUTHORITY
EAST HARTFORD, TOWN OF

EAST HAVEN PUBLIC LIBRARY
EAST LYME, TOWN OF
EAST WINDSOR HOUSING AUTHORITY
EAST WINDSOR, TOWN OF
EASTER SEAL REHABILITATION CENTER OF GREATER WATERBURY
EASTFORD, TOWN OF
EDGERTON GARDEN CENTER INC
EDUCAITONAL RESOURCES INC
EL HOGAR DEL FUTURO
ELLINGTON, TOWN OF
ENFIELD HOUSING AUTHORITY
ENFIELD, TOWN OF
ESSEX, TOWN OF

FAIR HAVEN COMMUNITY HEALTH CLINIC
FAIRFIELD HOUSING AUTHORITY
FAIRFIELD HOUSING SITE DEVELOPMENT AGENCY
FAIRFIELD, TOWN OF
FARMINGTON VALLEY ARTS CENTER
FARMINGTON, TOWN OF
FATHER NADOLNY GOOD NEWS FUND
FRANKLIN, TOWN OF

GILBERT SCHOOL
GILEAD HOUSE
GOODSPEED OPERA HOUSE FOUNDATION
GOSHEN, TOWN OF
GRANBY HOMES FOR SENIOR CITIZENS
GRANBY HOUSING SITE DEVELOPMENT AGENCY
GRANBY, TOWN OF
GREATER NORWALK COMMUNITY COUNCIL
GREENWICH HOUSING AUTHORITY
GREENWICH, TOWN OF
GRISWOLD, TOWN OF
GROTON, TOWN OF
GUILFORD CENTER FOR CHILDREN
GUILFORD, TOWN OF

HALL NEIGHBORHOOD HOUSE
HALL NEIGHBORHOOD HOUSE INC
HAMDEN, TOWN OF
HAMPTON, TOWN OF
HARTFORD APARTMENT IMPROVEMENT PROGRAM
HARTFORD COALITION FOR EMERGENCY SHELTERS
HARWINTON, TOWN OF
HEBRON HOUSING AUTHORITY
HEBRON, TOWN OF
HMS ROSE FOUNDATION
HOUSATONIC REGIONAL RESOURCES RECOVERY AUTHORITY
HOUSE OF BREAD INC

INTERLUDE INC
INTERNATIONAL INSTITUTE OF CONNECTICUT

KEELER TAVERN MUSEUM
KEENEY CULTURAL CENTER
KENT, TOWN OF
KILLINGLY HOUSING AUTHORITY
KILLINGLY, TOWN OF

LAKE HOUSATONIC AUTHORITY
LAUREL HOUSE
LEDYARD, TOWN OF
LIBRARY EXCHANGE AIDS PATRONS
LIFE HAVEN INC
LISBON HISTORICAL SOCIETY
LITCHFIELD HOUSING AUTHORITY
LITCHFIELD, TOWN OF
LITTLE THEATRE OF MANCHESTER INC
LOCKWOOD-MATTHEWS MUSEUM OF NORWALK
LYME HISTORICAL SOCIETY
LYME, TOWN OF

MADISON, TOWN OF
MANCHESTER HOUSING AUTHORITY
MANCHESTER LAND TRUST
MANCHESTER, TOWN OF
MANSFIELD HOUSING AUTHORITY
MANSFIELD, TOWN OF
MARLBOROUGH, TOWN OF
MATTABASSETT DISTRICT
MC CALL FOUNDATION
MERIDEN HOUSING AUTHORITY
MERIDEN YWCA
MERIDEN, CITY OF
METROPOLITAN DISTRICT
MID-FAIRFIELD CHILD GUIDANCE CENTER
MIDDLEBURY, TOWN OF
MIDDLETOWN HOUSING AUTHORITY
MIDDLETOWN, TOWN OF
MILFORD HOUSING AUTHORITY
MILFORD, TOWN OF
MILITARY MUSEUM OF SOUTHERN NEW ENGLAND
MOHONK HOUSE
MONROE, TOWN OF
MONTEVILLE, TOWN OF
MORRIS FOUNDATION
MOUNT OLIVE CHILD DEVELOPMENT CENTER
MUSEUM OF AMERICAN THEATRE
MY SISTERS' PLACE INC
MYSTIC SEAPORT MUSEUM INC

NAUGATUCK HOUSING AUTHORITY
NAUGATUCK, BOROUGH OF
NEHEMIAH HOUSING CORPORATION
NEIGHBORHOOD HOUSING SERVICE OF NORWALK
NEIGHBORHOOD PRESERVATION OF STAMFORD
NEW BRITAIN HOUSING SITE DEVELOPMENT AGENCY

NEW BRITAIN MUSEUM OF AMERICAN ART
NEW BRITAIN, CITY OF
NEW BRITIAN HOUSING AUTHORITY
NEW CANAAN HOUSING AUTHORITY
NEW CANAAN LIBRARY
NEW CANAAN, TOWN OF
NEW ENGLAND ADOLESCENT TREATMENT CENTER
NEW FAIRFIELD, TOWN OF
NEW HARTFORD, TOWN OF
NEW HAVEN FREE PUBLIC LIBRARY
NEW HAVEN HOUSING AUTHORITY
NEW HAVEN, CITY OF
NEW LONDON HOUSING AUTHORITY
NEW LONDON LEDGE LIGHTHOUSE FOUNDATION
NEW LONDON MARITIME SOCIETY
NEW LONDON, CITY OF
NEW MILFORD, TOWN OF
NEWINGTON HOUSING AUTHORITY
NEWINGTON, TOWN OF
NEWTOWN, BOROUGH OF
NEWTOWN, TOWN OF
NOAH WEBSTER FOUNDATION
NOANK HISTORICAL SOCIETY
NORFOLK, TOWN OF
NORTH BRANFORD HOUSING AUTHORITY
NORTH BRANFORD, TOWN OF
NORTH CANAAN, TOWN OF
NORTH CENTRAL CT MENTAL HEALTH SYSTEM
NORTH HAVEN HOUSING AUTHORITY
NORTH HAVEN, TOWN OF
NORTH STONINGTON, TOWN OF
NORTHEASTERN CT REGIONAL RESOURCE RECOVERY AUTHORITY
NORWALK ECONOMIC OPPORTUNITY NOW INC
NORWALK HOUSING AUTHORITY
NORWALK HOUSING SITE DEVELOPMENT AGENCY
NORWALK REDEVELOPMENT AGENCY
NORWALK, TOWN OF
NORWICH HOUSING AUTHORITY
NORWICH, TOWN OF

OLD SAYBROOK, TOWN OF
OLD STATE HOUSE

PATHWAYS INC
PERCEPTIONS PROGRAM
PLAINFIELD HOUSING AUTHORITY
PLAINFIELD, TOWN OF
PLAINVILLE GROUP HOME
PLAINVILLE, TOWN OF
PLYMOUTH HOUSING AUTHORITY
PLYMOUTH, TOWN OF
PORTLAND HOUSING AUTHORITY
PORTLAND, TOWN OF
PRESTON HOUSING AUTHORITY

PROJECT LEARN INC
PROJECT MORE INC
PUTNAM HOUSING AUTHORITY
PUTNAM, TOWN OF

REGIONAL NETWORK OF PROGRAMS
REGIONAL SCHOOL DISTRICT # 01
REGIONAL SCHOOL DISTRICT # 05
REGIONAL SCHOOL DISTRICT # 06
REGIONAL SCHOOL DISTRICT # 07
REGIONAL SCHOOL DISTRICT # 09
REGIONAL SCHOOL DISTRICT # 11
REGIONAL SCHOOL DISTRICT # 12
REGIONAL SCHOOL DISTRICT # 13
REGIONAL SCHOOL DISTRICT # 14
REGIONAL SCHOOL DISTRICT # 15
REGIONAL SCHOOL DISTRICT # 16
REGIONAL SCHOOL DISTRICT # 17
REGIONAL SCHOOL DISTRICT # 18
REGIONAL SCHOOL DISTRICT # 19
RESCUE
RIDGEFIELD, TOWN OF
RIVERFRONT RECAPTURE INC
ROCKY HILL HOUSING AUTHORITY
ROCKY HILL, TOWN OF
ROSE CITY COMMUNITY LAND TRUST
RURAL HOMES

SALEM, TOWN OF
SALISBURY, TOWN OF
SCOTLAND, TOWN OF
SECOND CONGREGATIONAL CHURCH OF COVENTRY
SELF INC
SEYMOUR, TOWN OF
SHARON, TOWN OF
SHELTER FOR WOMEN INC
SHELTON HOUSING AUTHORITY
SHERMAN LIBRARY
SHERMAN, TOWN OF
SIMSBURY HOUSING AUTHORITY
SOCIETY FOR THE PRESERVATION OF NEW ENGLAND ANTIQUITIES
SOMERS HOUSING AUTHORITY
SOMERS, TOWN OF
SOUTH WINDSOR HOUSING AUTHORITY
SOUTH WINDSOR, TOWN OF
SOUTHINGTON, TOWN OF
SPRAGUE, TOWN OF
ST AGNES HOME
ST LUKE'S COMMUNITY SERVICES INC
ST VINCENT DE PAUL SOCIETY
STAFFORD HOUSING AUTHORITY
STAFFORD SPRINGS, TOWN OF
STAMFORD CENTER FOR THE ARTS
STAMFORD HOUSING AUTHORITY

STAMFORD, CITY OF
STERLING, TOWN OF
STONINGTON, BOROUGH OF
STONINGTON, TOWN OF
STRATFORD HOUSING AUTHORITY
STRATFORD HOUSING AUTHORITY
STRATFORD, CITY OF
SUFFIELD, TOWN OF
SUNSHINE PROJECT INC
SUSAN B ANTHONY PROJECT

TEAM INC
THAMES VALLEY COUNCIL FOR COMMUNITY ACTION
THERE'S NO PLACE LIKE HOME
THOMASTON, TOWN OF
THOMPSON, TOWN OF
TOLLAND HOUSING AUTHORITY
TOLLAND, TOWN OF
TORRINGTON HOUSING AUTHORITY
TORRINGTON YMCA
TORRINGTON, TOWN OF
TRUMBULL, TOWN OF

UNION, TOWN OF
UNITED COMMUNITY SERVICES INC
UNIVERSITY OF BRIDGEPORT

VALLEY RAILROAD CO., ESSEX
VERNON HOUSING AUTHORITY
VERNON, TOWN OF
VITNAM CENTER
VOLUNTOWN, TOWN OF

WADSWORTH ANTHENEUM
WALLINGFORD HOUSING AUTHORITY
WALLINGFORD, TOWN OF
WATERBURY DEVELOPMENT AGENCY
WATERBURY HOUSING AUTHORITY
WATERBURY, CITY OF
WATERFORD COUNTRY SCHOOL
WATERFORD PUBLIC LIBRARY
WATERTOWN HOUSING AUTHORITY
WATERTOWN, TOWN OF
WESLEYAN UNIVERSITY
WEST HARTFORD INTERFAITH COALTION
WEST HARTFORD, TOWN OF
WEST HAVEN COMMUNITY HOUSE ASSOCIATION INC
WEST HAVEN, CITY OF
WESTPORT HISTORICAL SOCIETY
WESTPORT, TOWN OF
WETHERSFIELD HOUSING AUTHORITY
WETHERSFIELD, TOWN OF
WHEELER CLINIC
WHEELER CLINIC

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WILLIMANTIC HOUSING AUTHORITY
WILLINGTON, TOWN OF
WILTON, TOWN OF
WINCHESTER HOUSING AUTHORITY
WINCHESTER, TOWN OF
WINDHAM TEXTILE & HISTORY MUSEUM
WINDHAM, TOWN OF
WINDSOR HOUSING AUTHORITY
WINDSOR LOCKS, TOWN OF
WINDSOR, TOWN OF
WOLCOTT, TOWN OF
WOMEN'S CENTER, THE
WOODBURY, TOWN OF
WOODSTOCK HOUSING AUTHORITY
WOODSTOCK, TOWN OF

YALE UNIVERSITY
YOUTH CONTINUUM OF TRI-RYC INC

BRIDGES, PIPES AND CONCRETE: CREATING THE WILL TO PAY FOR INFRASTRUCTURE

The problem, regardless of growth, is where to spend ever-limited resources. Some places are struggling successfully.

Cleveland's bridges, streets and water pipes were falling apart, along with its economy. With its population and that of its county in decline, the Rust Belt city faced the formidable task of finding the leadership and the funds to rebuild, repair and replace its corroding and outmoded infrastructure.

In fast-growing Raleigh, North Carolina, where the population in the city as well as its environs is growing explosively, the challenge has been to invest ahead of tomorrow's demand, to pay for the four-lane highways, expanded sewers and new water treatment plants that could keep pace with and maintain the city's growth.

Seattle and the four counties that make up the Puget Sound region sit on the horns of both dilemmas. The fast-growing counties and slowed-down city are saddled with the city's deteriorating infrastructure as well as the counties' demands for new roads and fire stations for a population that should grow by half a million more in the next decade. As in other older, urban environments, pressing social issues divert dollars away from infrastructure.

These tales of three cities, expanded in the three-part report that follows, underscore the difficult and varied political pressures local governments face in maintaining and investing in infrastructure, which is the basis for attracting or maintaining economic growth.

"Infrastructure isn't sexy. It isn't like a domed stadium or a microchip road peppered with computer companies," says Ohio Senator Michael White, a Democratic candidate for mayor in Cleveland. "You never miss your water until the well runs dry."

Infrastructure is also enormously expensive. Nationally, this year's need is expected to be double the $45 billion spent in 1985 for new and upgraded infrastructure, according to the National Council on Public Works Improvement.

On a local level, the figures are equally formidable. In the past decade, as Raleigh's population grew from 150,000 to nearly 200,000, voters in that city approved $165 million in bonds and the spending of nearly one-fourth of the combined capital and operating budget on infrastructure.

Creating the political will to make such investments—as well as failing to—is the subject the tales from three cities explore. The reports underscore observations Nancy Rutledge makes about cities that have successfully financed infrastructure. The executive director of the now-disbanded national public-works council says that three things are essential to creating citizen backing for infrastructure investment: an elected official who champions the cause, a business community that helps or leads the charge, and a capital planning process that systematically sets priorities for future investment.

Linda Birch illustration

RALEIGH: KEEPING UP WITH GROWTH

So far, there are no building moratoriums because of limited sewer capacity, and no citizen revolts because of gridlocked roads.

By Penelope Lemov

When Sarah Wilson moved to Raleigh, North Carolina, 20 years ago, she and her family struggled to find housing. IBM and other major corporations were opening offices in a new research and development complex called Research Triangle Park, about two miles from Raleigh. Newly transferred employees were gobbling up existing apartments and homes in the sleepy state capital. When the Wilsons finally found shelter, it was in the relatively undeveloped northern part of the city. The big house atop the hill on their street was a family estate; cows grazed in nearby pastures.

North Raleigh today is a sea of single-family houses, apartments, office buildings and shopping centers. The area is crisscrossed by four-lane highways that head north and east to further development, and south and west to downtown Raleigh, an international airport, the research park, and Durham and Chapel Hill, which also feed off and into the research park. The house on the hill is a restaurant, and the cows, notes Wilson, an assistant in the public-affairs office of Raleigh's city manager, are a memory.

Like other Sun Belt cities that have witnessed the arrival in their regions of high-tech research facilities, Raleigh is booming. The unemployment rate hovers around 3 percent. The total value of property has increased 15 percent a year over the past eight years. The population of the city, which is also home to North Carolina State University, has nearly doubled in 20 years, rising from 122,000 people in 1970 to an estimated 218,000 in 1988.

But unlike many fast-growing Sun Belt cities, Raleigh has managed, with minor fiscal bumps and political bruises, to pace the building of infrastructure to its growth. The future may be rougher going, but so far there have been no building moratoriums because of limited sewer capacity, and no citizen revolts because of gridlocked roads. Traffic is considered heavy when drivers wait at an intersection for more than one change of lights or have to slow below the speed limit on highways.

"We've tried to stay ahead of crises. People in this city want to have good-quality infrastructure, and they have invested heavily in it through budget and bond approvals," says City Manager Dempsey E. Benton Jr. Since 1980, Raleigh voters have authorized a total of $165 million worth of bonds to build local streets, roads in and out of the city (traditionally a state responsibility), parking facilities, parks, sewers, an addition to an auditorium and, most recently, a baseball stadium (as yet unbuilt).

Voters have gone along with budgets that apportion 24 percent of revenues for capital improvements. The property tax, following a revaluation of real estate in 1984, had been creeping up by about a penny every other year and increased this year by 6 cents to 72 cents per $100 of property valuation. Also, developers have begun to pay impact fees to cover a share (about 10 percent) of the cost of roads and open space in areas in which they build.

Two things have made such financing possible. One is the nature of the population that's been arriving in Raleigh for the past 20 years: well-educated, white-collar professionals, many from cities where the infrastructure has deteriorated. "They let us know that they didn't want that to happen in Raleigh," Benton says. "They encouraged us to invest money in infrastructure."

The other reason is a political process that keeps voters informed about and involved with infrastructure issues. The process, first used in 1979, starts with a five-year capital improvements plan that inventories existing infrastructure and identifies projects for improvement or expansion. "It is a working document that guides the city administration in scheduling and constructing facilities in Raleigh," says Benton. It is also a document that is debated by the city council during both pre-budget and budget hearings. Projects that will be funded by the budget, and bigger projects that will be funded by bonds, are duly noted and discussed. They are also presented for discussion and comment to the city's 18 citizen-advisory committees.

"It's a never-ending process. There are occasions when we say we should have worked harder in informing people, but we have a commitment to an open process. It's the people's business we're about. We don't cut deals in back rooms," says Mayor Avery Upchurch.

Major infrastructure projects are designed to be citywide. Each time park or transportation projects are planned, each part of the city gets a share of the improvements. "That, to me, has been one of the elements built into our success," says Upchurch.

Once a project is approved, Benton's office moves quickly to start construction within 18 months. "We have a strong emphasis on a short turnaround time between appropriation and availability of services," Benton says. "We want to have credibility when we go back to our voters for the next project."

Priorities for funding projects are set by the city council. For the most part, infrastructure is Raleigh's responsibility; social welfare and education are Wake County's. Officials in both governments coordinate their efforts to tap public willingness to finance major programs. "Raleigh represents 55 percent of Wake County voters, so we don't want to go to voters at the same time for approval of competing issues," Benton says. Accordingly, the city went to its voters in 1987 with a $97.5 million bond referendum for roads, parks and utilities; the county clocked in last year with a $125 million referendum on education. Both passed with more than 70 percent of the vote.

The city apportions $2.2 million of its $164-million-a-year capital and operating budget to such social programs as Meals on Wheels and assistance for the homeless. With a healthy and growing economy, however, Raleigh's social problems are not on a par with those of such large cities as New York. They have not, in short, had an impact on the city's ability to fund infrastructure during the 1980s.

The public is kept informed and 'we don't cut deals in back rooms,' says Mayor Avery Upchurch.

That could change in the coming decade, not because the economy will falter or social problems increase, but because the city faces growing restrictions on its ability to raise revenue. The state legislature has rescinded the authority of local governments to tax personal property. The state funds apportioned to the city of Raleigh to cover that revenue loss, says Benton, do not accommodate the city's rate of growth, which direct taxation would have covered. In addition, the state mandated an increase in retirement benefits for law enforcement officers. "In the past, such mandates were accompanied by revenue to cover the mandate. They didn't do that this time," Upchurch says.

One way the city is attempting to make up for the decrease in revenue is through increased user fees on such items as automobile ownership decals and by imposing impact fees on developers. These impact fees, which went into effect after three years of negotiation, are assessed on developers and builders based on the size and type of project they are constructing.

Although the development community has, so far, been fairly sanguine about them, the fees represent a potential fiscal shoal for the city. Not one of Raleigh's neighbors in the Research Triangle area imposes such fees. There is concern that developers could move out of Raleigh to other nearby cities, where it is less expensive to build. "We depend on our tax base to fund government obligation bonds. We need development to maintain our growth," says Benton of the city's sensitivity to the fees.

Smedes York, mayor of Raleigh from 1978 to 1983 and president of York Construction Co., notes that the development community does not "embrace the fees, but there hasn't been a mass exodus. The reason Raleigh could put the fees in is that there was a strong market here. There's some overbuilding now, and that could make the fees less palatable."

Historically, Raleigh's development community has cooperated with the city to help finance infrastructure. In 1985, for instance, developers agreed to pay sewer hookup fees in advance, thus financing one-third of the $9.1 million cost of building 17 miles worth of new sewer lines and a pumping station. This relatively quick fix helped work out a compromise on another sewer problem. Private developers had begun constructing their own small sewer plants to serve developments built beyond Raleigh's sewer service area. With the financing in hand to expand the sewer system, city officials were able to work out arrangements with the developers to abandon their private plants and connect to city sewer lines once those lines are constructed.

If there's one criticism developers like York have about Raleigh's infrastructure program, it is that the city has gotten bogged down in regulation in the past few years, and so has failed to move ahead quickly with such projects as the minor-league baseball stadium. "They also let an arena get away from them," says York. "The city council needs to move out in front on progressive issues."

Raleigh's capital improvement future is also clouded by the growing need for regional solutions to many infrastructure problems, such as solid-waste disposal and watershed protection. The region ranks in the top 20 for its state-of-the-art regional planning, claims Chapel Hill Mayor Jonathan Howes, who was president of the National Association of Regional Councils. On the other hand, he adds, "like most parts of the country, regional implementation is primitive. We in local government are reluctant to grant power or decision making to supralocal bodies."

Meanwhile, Raleigh's mayor plays an active role on committees and projects that are part of regional council-of-governments efforts. He also is actively lobbying state and federal governments for infrastructure assistance. And he and the city council are looking at ways to adjust the budget. "We may have to cut back, but fortunately, many of the improvements we made during the 1980s will carry us into the next decade." ☐

Karen Tam photograph

DEVELOPMENT

CLEVELAND: COMING OFF THE BOTTOM

County and city both are still declining, but a savvy coalition is finding the money for rebuilding. Can it keep ahead of the decay?

By Cynthia Kyle

Water pipes in Cleveland, laid before 1955, were corroded and clogged to the point that service to hundreds of customers was being cut off at peak demand hours. The condition of the pipes threatened the city's response to fires, and a county judge declared the system a danger to human health and safety. So severe were sewer maintenance cutbacks that the city could respond only to emergencies: street cave-ins or reports of sewage flooding into basements. A third of the bridges in the city's care needed major work; so did a like number of streets. Even the roof of Cleveland's handsome granite city hall leaked.

Years of neglect, refusal to raise taxes and political bickering had taken their toll on the Lake Erie city once touted as the "best location in the nation" but since derided as "the mistake on the lake." Unemployment was up and the population, in surrounding Cuyahoga County as well as in the city, was shrinking dramatically.

Cleveland's financial bookkeeping was declared unauditable. Locked out of the capital markets by its default in 1978—the first default of a major U.S. city since the Depression—Cleveland could barely come up with its share of the money to match federal and state funds available for infrastructure overhaul.

Finally, in 1979, the city endorsed an income tax increase; elected George V. Voinovich, a Republican and former lieutenant governor, as mayor; and set out to reclaim itself. Riding a business-backed campaign into city hall, Voinovich called himself the "private-public partnership mayor."

Indeed, the day after his election, executives from eight major accounting firms and four major corporations agreed to a pro bono financial audit of the city. The verdict, after 11 weeks of work: $110 million in accumulated budget deficits that had to be paid off somehow.

In the next two years, 90 loaned executives would recommend 650 ways for the city to operate more efficiently, and Cleveland voters would approve yet another income tax increase. Half of the new tax, set at 2 percent, would retire the city's debt. The other half would finance infrastructure repair. A systematic process for setting priorities—a five-year capital improvement plan, updated every year—was put in place. Wall Street responded by boosting the city's credit rating in the summer of 1981, and the stage was set to rebuild.

Repair or replacement of fire stations, some dating back as far as 1875, came first, because of their impact on life and safety. But fixing the leaky roofs of recreation center buildings got high priority, too, because the public wanted their indoor swimming pools and other facilities; it was a way of building public support for the infrastructure repair effort. All totaled, the first five-year plan, covering the 1981-1986 period, identified $400 million in deferred maintenance needs. City hall's roof was fixed in 1985.

Reconstruction is now under way on the city's ancient Division Avenue water plant, built in 1915 and formally designated as in "hazardous condition." The price tag: $102 million.

In another three years, the city expects to rehab or replace 17 Cuyahoga River bridges that connect major industrial routes. The city is starting replacement of another 17 bridges, mostly arterial railroad crossings constructed in the 1920s.

"We're trying to catch up," says Richard Halishak, commissioner of engineering and construction. "Sometimes we close more than we open." As of March, four bridges remained closed because of their condition and five more bridges were closed for construction.

The latest five-year plan includes neighborhood development projects for the first time: demolition of vacant and vandalized buildings that can't be saved and renovation and code enforcement of those that can, in both residential and commercial districts. The overall price tag for the five years: $1.01 billion. Some $740 million of it will come from local sources, the rest from federal programs and the state. That the city had to hit bottom before it could pull itself up by the bootstraps "is an unfortunate statement of fact," says Finance Director Charles Brown.

George Peterson, a researcher at the Urban Institute, which in 1979 found Cleveland's infrastructure among the nation's worst, is impressed by the city's transformation. "What's unique about Cleveland is the human network that's been able to keep infrastructure at the top of its priorities," he says.

The hub of the network, an organization known as Build Up Greater Cleveland, was formed in 1983 by the Greater Cleveland Growth Association, a regional chamber of commerce with 8,500 member companies in seven northeastern Ohio counties. Major financing came from Cleveland-based charitable foundations.

What is notable about Build Up, as explained by its director, Walter Olson, a retired National Aeronautics and Space Administration executive, is the way its members

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were selected. "We picked positions, then we asked the people to serve. No matter who the people were, we needed the position."

Among those named to Build Up's policy committee through this bald but savvy strategy: the president of the Cuyahoga county commission, a Democrat; the president of the Cleveland city council, a Democrat; the Cuyahoga county engineer, who has authority over all suburban road and bridge-repaving projects; Mayor Voinovich and key financial and public-works members of his cabinet; a bank officer who handled government bond projects; the vice president of a major oil company, one of the city's leading employers; and U.S. Representative Louis Stokes, a Democrat with 20 years of service in Congress and a key seat on the House Appropriations Committee.

The city had to hit bottom before it could pull itself up, says Finance Director Charles Brown.

Stokes believes that Cleveland found the political will to deal with its problems because of "the growing maturity of the business community in terms of their relationship with the political infrastructure of the city.... Whether we're Republicans or Democrats, it's our city."

"United we stand and make progress," says Voinovich. "Divided we weren't getting very far."

Through its collective lobbying efforts, Build Up has nailed down such revenue sources as $122.4 million in federal funds for roads and bridges, $81 million in federal funds for transit, $22.6 million in federal wastewater construction grants and $40 million in federal transportation funds as the city's share of a state allocation. "We looked everywhere we could for money," says Olson. "We'd go to a committee in Washington and say 'Here's our plan and here's the expected federal role. Who expects it? We expect it.'"

"It also didn't hurt to have a Republican at city hall and a Republican in the White House," says Norman Krumholz, professor of urban planning at Cleveland State University and former director of Cleveland's planning commission.

Lobbying in Columbus and around the state, with some 40 polished speakers, Build Up helped persuade Ohio voters to approve a $1.2 billion bond issue in 1987 to finance infrastructure work. The proceeds of the issue promise $14.5 million annually for the next 10 years for Cuyahoga County improvements.

Cleveland helped itself by raising water rates and income taxes—though efforts in 1984 for a third income tax increase failed—and by repeated forays into the bond market, once its credit was re-established. It sold $153.3 million in waterworks improvement bonds in 1987, the largest offering in the city's history. Both the city and Cuyahoga County took advantage of state legislation authorizing increases in local motor vehicle license fees.

To be sure, there is some grumbling. Dennis Kucinich, the Democrat who was mayor during the city's default, complains that political leaders and private businesses are too cozy. "The private-public partnership is two hands in the taxpayers' pockets instead of one. In Cleveland, business is the government."

Other Democrats cheer. "If we don't make repairs, if we don't replace the old, [corporate chiefs] will say goodbye, and with them will go thousands of jobs," says Senator Michael White, a Democratic candidate for mayor. During 1988, the Greater Cleveland Growth Association recorded new corporate investment of $98 million and nearly 1,500 new jobs. "Without new roads and bridges, people would turn elsewhere to establish their businesses," says another mayoral hopeful, Cuyahoga County Commissioner Timothy Hagan. "You can sell that position without selling your soul." He thinks the private-public partnership and its accompanying tax increases were more politically palatable because the taxes were levied for specific rather than general purposes and their need was undebatable.

Now, uncertainty confronts the city. Voinovich, the city's longest-serving mayor, who lost his 1988 bid for U.S. Senate, must decide before summer's end whether he will seek re-election. The flow of new federal money is, at best, problematic, whatever the city's clout in Washington. The Environmental Protection Agency is threatening to impose an estimated $20 million in sanctions unless the legislature empowers Cleveland to start an automotive emissions testing plan to curb carbon monoxide pollution. Penalties could include a ban on industrial construction and the loss of federal sewer funds.

Economic experts warn of recession, although Voinovich thinks the city's more diversified economy means that "our back will not be broken like it was in the '80s." The city's population is still declining; a Cleveland State University researcher projects a further decrease of some 100,000 by 2005, from the 1986 Census Bureau estimate of 536,000. The suburban count could continue to drop, too, something that is not happening in most other old Rust Belt areas.

"You can ask: If we've been so good at raising money, why hasn't the problem gone away?" Olson says. "That simply reflects the fact that . . . the infrastructure is eroding as fast as you fix it." ☐

Barney Taxel photograph

DEVELOPMENT

SEATTLE: DEFEATED BY THE SPRAWL

A booming population, spreading outward with ever-decreasing density, tests the will and the resources to provide basic needs.

By John Herbers

The Puget Sound region in and around Seattle has long provided one of the most livable urban and rural environments in America. In recent years, it has become a vibrant economic unit as well, covering 6,294 square miles of scenic land in four counties that are home to 2.6 million people—a kind of paradise on earth, many of them will tell you, with fingers of land stretching into blue waters, the grade of the hills providing the maximum view of the emerald landscape, and everywhere tapered evergreens bathed by mist. On a clear day, the snow-covered peak of Mount Rainier rises majestically on the horizon.

But wait. There is trouble in paradise. Another half a million people are expected by the year 2000, and residents already are finding they can no longer get to work or to the lakes and mountains in 20 minutes, or even an hour. Bookstores are doing a booming business among those who want more than newspapers to read in traffic jams. Powerful no-growth movements are under way among citizens in rural and urban areas alike.

Government, business and civic leaders are furiously looking for ways to control the growth without wiping it out and to build and maintain the streets, roads, bridges, ferries, public buildings, and water and sewer systems needed right now. One statistic will serve to exemplify the growing needs and the lack of adequate response. The miles traveled on highways in King County, the region's most congested, more than doubled from 1965 to 1985, from 18 million to 42 million, yet the amount spent for capital improvements has declined (in dollars of constant value) from $390 million to $300 million, and for maintenance from $450 million to $350 million. Tax revenues were diverted to more politically popular programs, education among them. The gap between miles traveled and money spent continues to widen.

In the Puget Sound region, the difficulty is not the lack of resources or of a political culture that supports governmental action. Indeed, William Stafford, director of intergovernmental relations for Seattle, points out that the vote in the Puget Sound region carried the state for Democratic presidential candidate Michael Dukakis. Proposals calling for ambitious new tax levies to wipe out the infrastructure deficit come from various leadership groups, including the business community.

The trouble lies with the fractured system of government, which has had its weaknesses magnified by the decline in aid from the federal government. In addition to the four county governments, the region encompasses 71 municipalities, more than 1,000 special-service districts and three Indian reservations, all with taxing authority and all in the business of delivering services.

Only the state government is in a position to step in and impose regionwide solutions, but the state has been more hindrance than help. Washington's government resembles those of most Southern states of two decades ago, with a constitutionally weak governor's office and a strong legislature dominated by rural interests. The legislature is particularly restrictive about what taxes local governments may raise and how the money is spent. The urban areas of western Washington, which pay one-third of the gasoline taxes that go into the state's treasury, get only about 6 percent back.

As the pressure has mounted on officials in the Puget Sound region, they have become quarrelsome and further divided on approaches to solving their problems. Seattle's Democratic mayor, Charles Royer, who in the past 11 years has presided over a downtown building boom and construction of thousands of housing units for poor and moderate-income residents, has wearily announced that he will not run for re-election when his term ends later this year. He has watched Seattle lose its supremacy, and much of its political clout, both in the legislature and within the region, as the population around it has burgeoned while the city has struggled to stem its decline.

Royer says the governmental structure in the Puget Sound area is like the state's complex, inequitable tax structure: "Each is a patchwork so out of date and out of balance that it cannot meet the demands of our region."

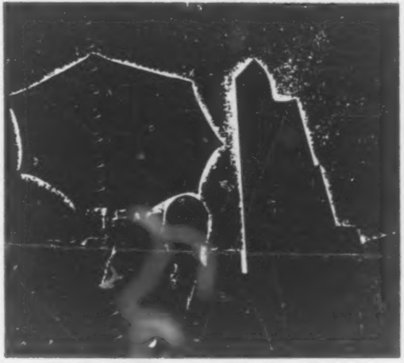
Life isn't paradise either for Tim Hill, the elected executive of King County, who has the same powers as a strong mayor. As head of the largest unit of government in the region, Hill would be expected to take the lead in achieving a regional approach in building and maintaining infrastructure. But he is constantly on the defensive and under attack from the county's 29 municipalities and his own council members.

Under state law, county taxing authority is very limited. Counties cannot levy business and occupation taxes or utility taxes, as municipalities are permitted to do. Instead, King County keeps raising the sales tax to its allowable limits, now above 8 percent, while the municipalities attack it for spending money collected within their borders to provide urban services to residents of unincorporated areas.

The situation is further complicated by a proliferation of special-service districts.

Aside from the state, the only overarching agency that could make sense out of this crazy quilt of governments is the Puget Sound Council of Governments, but it has no power except that voluntarily delegated to it by its component governments. Its only significant power now is planning an areawide transportation system. Yet the King County council, over Hill's objections, recently withdrew most of its financial support for the organization because, according to County Council Chairman Gary Grant, it was not getting anything done "on the tough issues of forging regional mandates." Hill, a moderate Republican, thinks that the action only hurt efforts for regional agreement.

If that were not enough, residents of unincorporated urban areas have been clamoring to be annexed to towns and cities because the county is unable to pay for all the urban services they want, including police protection. Hill would like to see that happen, because the county could then focus on providing traditional county services such as health care and jails. But members of the county council are opposed because they would lose many of their constituents.



Tim Hill, King County's elected executive, tries for a regional approach but rarely succeeds.

Against this backdrop, there are symbols that show the need and the seeming inability of government to meet it.

In Seattle, there is a narrow, ancient bridge on First Avenue that has been in need of replacement as long as most people can remember. It has been the cause of huge traffic jams and several deaths. It is owned and operated by the state as part of its highway system, but neither state nor local officials have ever found the funds, now estimated at about $100 million, to replace it. Nor can the city put its hands on enough money to properly maintain its streets, according to Ken Bounds, assistant city budget director for infrastructure.

A few miles north of Seattle, in Snohomish County, there is a new 1,078-acre, Japanese-planned community called Mill Creek. The development has brought severe traffic tie-ups on nearby highways. At least 10 development companies are planning similarly large housing communities in rural areas stretching from Snohomish County to south of Tacoma.

In the northern part of King County, there was a heated controversy over plans for 7,500 new homes and 2,500 apartments. The county, following a master plan of two years ago that called for higher densities, wanted to zone the land at one housing unit per acre. The compromise ultimately reached, balancing the demands of builders, slow-growth rural residents and environmentalists, permitted the development but zoned the land beyond it at one house every five acres.

Meanwhile, back in Seattle and other urban areas, citizens have gotten up ballot initiatives which, if approved, would slow development by putting a cap on construction. This, according to Royer and others, would only force more growth into the outlying, low-density part of the region, whose infrastructure needs are not being met now.

Still, there is so much energy, innovation and public interest throughout the region that a workable plan for infrastructure could well emerge as a matter of pure necessity. The various governments have taken a partially regional approach to sewage treatment and disposal through an agency called Metro. Tunnels are being built under downtown Seattle for buses and ultimately light trains. Multiple plans are on the boards for solving the infrastructure crisis, although there is no overall master plan the interests can agree to.

For now, the only relief in sight seems to be another, almost certain increase by the state in the gasoline tax and a change in the distribution formula. Bills that would add anywhere from 3 to 9 cents per gallon to the present 18-cent levy are under debate in Olympia. But whatever the increase, it will be far from all that is needed.

What the citizens and officials of the Puget Sound region have not focused on is the real nature of their infrastructure problem. It goes beyond simply finding the political will to raise taxes or even the more difficult task of modernizing obsolete governmental structures. The underlying question is whether government can, in fact, be expected to maintain and repair the old infrastructure in aging, dense cities and simultaneously build the new facilities in communities of very low density that are expanding almost without restraint.

The number of persons per housing unit shrinks every year, with fewer people getting or staying married, more single-parent homes and fewer children. The density of housing units per square mile also shrinks, as development reaches into the countryside. The greater the distance between households and the smaller the households, the more bridges, the more miles of asphalt and concrete, pipes and wire that will be needed. This is the fundamental problem that countless areas across the nation, along with the Puget Sound region, have not yet confronted. ☐

Matthew McVay/Picture Group photograph

ESSAYS ON ISSUES

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SEPTEMBER 1986
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Chicago Fed Letter

Rx for productivity: Build infrastructure

A six-car collision on Tampa's two-lane Howard Frankland Bridge—the locals call it the "Frankenstein"—causes a three-hour traffic jam during rush hour. A dam bursts near Toccoa, Georgia, killing thirty-nine residents—mostly children—of a tiny Bible college. A bridge collapses on Interstate 95 in Connecticut, hurling six people into the river some 75 feet below, killing three and injuring several others.

Such accidents and disasters happen almost daily in the United States. They are outward signs of a growing affliction—the decay of our national infrastructure. But not only safety and convenience are affected. There are deeper implications of this national neglect for the health of the U.S. economy. Indeed, as Bill Clinton, Governor of Arkansas, recently wrote, "America is falling apart, literally. Federal budget pressures and changes in the Federal tax law in the 1980s have steepened a decline in public works spending that dates to the 1950s."[1]

This *Letter* looks at recent trends in public works expenditures and relates the fall-off in such spending with the productivity slowdown that became evident in the United States around 1970. The decline in public capital spending—on dams, highways, sewers, mass transit, etc.—relative to employment and private investment in plant and machinery forces private business to absorb higher costs, and thereby lowers productivity. And lower productivity, sooner or later, means a lower standard of living.

A stronger commitment to America's infrastructure by the public sector is necessary for at least two reasons. First, a well-maintained public works system contributes to an expanding, robust economy. Second, directly and indirectly, it contributes to an improved standard of living.

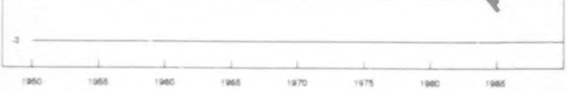
A check-up

On the basis of most external appearances, the economy's health is robust. We are experiencing an expansion of output that is progressing into its sixth year; economists are raising their forecasts for this year's growth rate of gross national product (GNP); we see surging employment and a declining unemployment rate. To be sure, we see some threats of inflation, but not the inflation fever of other periods.

A complete physical examination, however, produces evidence of economic atrophy. The growth of output that is not explained by increases in labor and private capital inputs—generally called "total factor productivity"—has slumped during the last decade and a half. Indeed, the annual growth rate of total factor productivity in the private business economy has plummeted from 1.5% from 1951 to 1960 and 1.8% from 1961 to 1970 to 0.8% in the 1970s and a dismal 0.7% in the first half of the 1980s.

When an economy begins to produce less per worker, as has been the experience in the United States of late, commonsense suggests various possible solutions. Households can scale back consumption purchases in line with reduced income growth. Firms can reduce expenditures on capital goods in the face of lower profit margins. Or the government can reduce its own spending on goods and services (consumption spending), leaving a larger slice of output to be allocated to competing private sector needs. However, none of these resolutions have occurred, or at least have not occurred sufficiently enough to match the diminished availability of domestically produced goods and services.

Instead, households, businesses, and the government have saved less and borrowed more in the attempt to consume, invest, and finance public spending in excess of their income, cash flow, and tax revenue.



After averaging 9% of GNP during the 1960s, the private savings rate fell to 8.3% during the 1970s and even lower, to 6.2%, during the first half of the 1980s. Also, there has been a high budget deficit as the government sector's outlays exceeded the pace set by tax revenues. During the last years of the Carter Administration and throughout the Reagan Administration, budget deficits ballooned, with the excess of spending over revenues peaking at 5.4% of GNP in 1984.

In turn, the national attempt to spend beyond our present means has forced up real interest rates as well as caused a trade deficit in the international accounts. Higher interest rates work to choke off private expenditure, particularly on durable goods, thereby lowering the demand for borrowed funds. At the same time, higher domestic interest rates—relative to foreign rates—also attracted foreign capital. This had the desirable effect of allowing a higher private investment rate, thereby enhancing future productive capacity, than would have occurred in an economy closed off from international capital markets. Still, this has resulted in a large liability to the rest of the world. Indeed, by most accounts, the United States went from being the world's largest creditor to the world's largest debtor in less than a decade.

The ultimate consequence of the productivity disease then will be a lower standard of living as we pay back the debt held by foreigners.

Previous diagnoses

Prior studies of the fall-off in productivity have centered on a relatively small number of potential causes. A surge in aggregate productivity can be expected whenever resources are shifted from less to more productive sectors of the economy. The migration of labor from farm to nonfarm occupations had such an effect, but mostly came to a halt by the mid 1960s. Certain economists, most notably Zvi Griliches of Harvard University, have emphasized a general slowing of expenditures on research and development and a related slowing of technological change.

of	1950-85	1950-70	1971-85
Productivity	1.5%	2.0%	0.8%
Public capital	3.0%	4.1%	1.6%
Public capital relative to private inputs	1.1%	2.4%	-0.6%
Capacity utilization	0.2%	0.3%	0.1%

But, the combination of these factors does not go far enough in explaining the productivity decline. The Bureau of Labor Statistics, for example, estimates that these factors probably account for only one-fourth or so of the slower productivity growth in the private economy. Lower rates of capacity utilization also may explain some of the reduction in total factor productivity; after averaging 84.1% during 1951 to 1970, the rate of capacity utilization fell to 79.5% in the period 1971 to 1985. But changes in capacity utilization rates, largely driven by erratic fluctuations in aggregate demand for goods and services and transitory technological shocks, are more likely to explain short-term, rather than long-term movements in productivity.

A new diagnosis

One place to search for a plausible reason for the productivity decline is in the government accounts—how the government gets and spends its money. Many have insisted that the financial status of the public sector—the budget deficit and consequent creation of government bonds—may play an important role in influencing the economy's performance. Specifically, it is argued that high public sector bond issuance forces up real interest rates and drives down the new private investment spending that is essential for fostering economic growth and technological improvement.

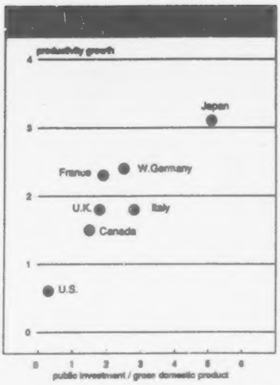
I suggest, however, that it is more reasonable to look at the physical aspects of the government budget, at the distribution of government spending across various broad categories.

As it happens, there is a remarkable correlation between the level of total factor productivity and the level of the nonmilitary public capital stock over the last thirty-five years. My empirical results suggest that movements in public capital are capable of explaining a large portion of the longer term movements in productivity in the private sector over the period 1949 to 1985.[2]

Roughly, a one percentage point increase in the level of the net stock of public capital relative to the level of private sector inputs of labor and capital brings forth a one-third of one percentage point (.33) rise in productivity. Table 1 translates this result into an accounting mechanism for the growth rate of total factor productivity during the high-growth period 1950-70 and the subsequent low-growth period 1971-85. While productivity growth fell from 2% to 0.8% per year—a fall-off of 1.2 percentage points—the growth rate of the net stock of nonmilitary public capital shriveled from 4.1% to a mere 1.6% per annum. Even more strikingly, the growth rate of the public capital stock *relative to* a "combined" unit of private labor and capital went from a strongly positive 2.4% to a *negative* 0.6% in the slowdown period.

Multiplying the slump in the growth in public capital by the sensitivity of productivity to public capital growth—the previously mentioned 0.33—shows that fully (3.0) x (.33) = 1.0 percentage point of the total decline in productivity of 1.2 percentage points can be attributed to the neglect of infrastructure.

Figure 1 vividly illustrates the tight relationship between public nonmilitary capital and total factor productivity by comparing levels of total factor productivity and the stock of public structures and equipment after removing time trends. As is clearly demonstrated, this relationship holds for the period of rising productivity growth during the 1950s and 1960s as well as for that of falling productivity growth during the last decade and a half. And, as low productivity growth leads a low standard of living by the hand, insufficient investment in the economy's infrastructure will soon force individuals to trim their style of living; Senator Quentin Burdick of North Dakota warns, "We have produced a high standard of living, but we are beginning to see cracks in that high stand-



ard, and a less than adequate infrastructure has been identified as the cause."[3]

We would also expect that countries that sustain a high level of public investment relative to output would experience higher productivity growth than countries that do not invest in infrastructure. Figure 2 illustrates precisely this result, plotting combinations of annual growth rates of gross domestic output per employee hour and ratios of public investment spending to gross domestic output for the "G-7" countries over the period 1973-85. Japan has invested about 5.1% of output in public facilities and achieved productivity growth of 3.3%; at the other end of the spectrum we find the United States with a low public investment of 0.3% per year and low productivity growth of 0.6% per annum. At the same time, productivity growth in these countries was negatively related to government consumption spending.

While total government outlays relative to GNP have risen from 26% in the late 1950s to 35% in the middle of the 1980s, public nonmilitary capital expenditures have slid precipitously. Dana Huestis, President of Associated General Contractors of America, has stated in Congressional testimony, that "the infrastructure crisis is real. As a nation, we have not been investing enough in our public facilities to either keep up with new growth, or to rebuild and protect what is falling into disrepair."[4]

Thus, a root cause of the decline in the competitiveness of the United States in the international economy may be found in the low rate at which our country has chosen to add to its stock of highways, port facilities, airports, and other facilities which aid in the production and distribution of goods and services. Just as thoughtful athletes would not think of neglecting their health for fear of failing to compete well on the playing field, we as a country should be vitally concerned with the viability of our economic lifelines that enable us to meet the challenge of an increasingly competitive world marketplace.

In the words of Nancy Rutledge, Executive Director of the National Council on Public Works Improvement, "If we spend too little on public works...society loses more than the direct public cost. In the long run, our ability to compete in the international economy will be weakened, and our standard of living will suffer."[5] Nearly echoing her remarks, Peter Butkus, a public works manager for the State of Washington, has said that "good public works becomes the single most important thing that local governments can provide in the nation's effort to maintain and expand foreign trade and competitiveness."[6]

Prognosis

The chance for a recovery from a physical condition such as a minor hardening of human arteries is usually quite good if it is identified early enough, and the patient adopts a proper counting of calories, a good diet, and a certain amount of exercise. Similarly, given the stability of the relationship between the economy's infrastructure and the productivity of private factors of production, we may be confident that a more balanced distribution of public sector resources, shifting some from consumption and into capital accumulation, will rejuvenate the economy's lifelines.

Raising the level of public investment spending from its current abysmal level of less than one half a percent of GNP to a modest two percent—some 80 to 90 billion dollars per year—would work wonders, quite likely wonders comparable to those of modern medicine in dealing with human disease.

— David Alan Aschauer

---

[1] "America is Buckling and Leaking," *New York Times*, June 24, 1988.

[2] These estimates are contained in David Alan Aschauer, "Is Public Expenditure Productive?" Federal Reserve Bank of Chicago, working paper, in press.

[3] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, October 21, 1987.

[4] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, October 6, 1987.

[5] *Fragile Foundations*, National Council on Public Works Improvement, February 1988.

[6] Senate Hearings, Subcommittee on Water Resources, Transportation, and Infrastructure, November 4, 1987.

Karl A. Scheld, Senior Vice President and Director of Research; David R. Allardice, Vice President and Assistant Director of Research; Edward G. Nash, Editor.

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Fragile Foundations:
A Report on America's Public Works

Final Report to
the President and the Congress

National Council on Public Works Improvement

February 1988

National Council on Public Works Improvement

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Joseph M. Giglio, Chairman

Senior Managing Director of Public Finance for the investment banking firm of Bear, Stearns & Co., Inc. Born in Bayonne, New Jersey, he previously served as a cabinet officer under Governor Hugh Carey of the State of New York (1977). He was Chairman of the U.S. Senate Budget Committee's Private Sector Advisory Panel on Infrastructure Financing (1985-1987). He is a graduate of Rutgers University (1967), and holds master's degrees in public administration from New York University (1972) and in business from Columbia University (1977). Mr. Giglio was appointed to the Council by the President pro tempore of the U.S. Senate.

Peter C. Goldmark, Jr.

Former Executive Director of the Port Authority of New York and New Jersey (1977-1985), currently Group Vice President, Eastern Newspapers for the Times Mirror Company. Born in New York City, he served as Director of the Budget for the State of New York (1975-1977) and Secretary of Human Services for the Commonwealth of Massachusetts (1971-1975). He is a graduate of Harvard College (1962). Mr. Goldmark was appointed to the Council by the Speaker of the U.S. House of Representatives.

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Former Vice Chancellor for Administration of the Oregon State System of Higher Education (1969-1979), currently President of the City Council of Eugene, Oregon. Born in St. Paul, Minnesota, he previously served as Director of Environmental Protection for the State of Wisconsin (1966-1968) and Director of Finance and Administration for the State of Oregon (1959-1966). He is a graduate of Concordia College (1938) and holds a master's degree from the University of Oregon (1946). He was professor of political science at Willamette University (1949-1959) and at New York University (1946-1949). Mr. Holmer was appointed to the Council by President Reagan.

Lowell B. Jackson

Registered Professional Engineer, currently a private consultant in Aurora, Colorado. Born in Milwaukee, he served this past year as Chairman of the Executive Committee of the Transportation Research Board. He was Secretary of Transportation in the State of Wisconsin (1979-1981, 1983-1986) where he also served as Secretary of Labor (1981-1982), and was Director of the Colorado Department of Highways (1987). His civil engineering degrees are from Purdue University (1957, 1959), where he was a member of the faculty (1957-1965). He also was a tenured faculty member at the University of Wisconsin (1965-1978). Mr. Jackson was appointed to the Council by President Reagan.

Frieda K. Wallison

Partner in the law firm of Jones, Day, Reavis & Pogue. Born in New York City, she previously served as Executive Director and General Counsel of the Municipal Securities Rulemaking Board (1975-1978). She also was Special Counsel of the Securities and Exchange Commission (1975). She was a member of the National Council on Governmental Accounting, and now serves on the Governmental Accounting Standards Advisory Council. She is a graduate of Smith College (1963) and holds an LL.B. from Harvard University (1966). Mrs. Wallison was appointed to the Council by President Reagan.

Nancy S. Rutledge, Executive Director

Former Director of the Washington State Public Works Project (1982-1985). Prior to joining the Council, she was an investment banker with the firm of Seattle-Northwest Securities, Inc. (1985). Born in Olympia, Washington, she is a graduate of Pacific Lutheran University (1970) and holds a master's degree in public administration from the John F. Kennedy School of Government at Harvard University (1979).

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Preface

The National Council on Public Works Improvement (the "Council") was created by the Public Works Improvement Act of 1984 (P.L. 98-501) to assess the state of America's infrastructure. The results of that evaluation are presented in a three-part document, *Fragile Foundations: A Report on America's Public Works*.

- Part One summarizes the Council's findings and its conclusions about the capacity of the nation's infrastructure to support future economic growth. It also outlines the Council's proposed strategy for strengthening these facilities and restoring a clear commitment to the future.
- Part Two provides a synthesis of major themes from over 5000 pages of research material prepared for the Council during the past two years. All of the research findings were reviewed and commented on by a wide range of public works experts in dozens of working group meetings, public hearings, and other public forums.
- Part Three is an Appendix that analyzes the performance of eight major categories of public works.

The three parts of this report represent the Council's final submission to the President and the Congress. This document is Part One of that report.

The Council's first report, *The Nation's Public Works: Defining the Issues*, provided an overview of current knowledge and set a broad context for further discussion and research. The issues included public works needs, economics and finance, government roles, management and decision making, and technological innovation. That report was submitted to the President and the Congress in September 1986.

The second report took the form of a series of study papers commissioned by the Council from independent consultants on nine categories of public works facilities and services: highways, streets, roads, and bridges; airports and airways; mass transit; intermodal transportation; water resources; water supply; wastewater management; solid waste; and hazardous waste. Each paper addressed the main issues identified by the Council in its first report. In the final chapter of each paper, the consultants provided the Council with their own views on major policy options in that category. These recommendations were reviewed by the Council but have not necessarily been incorporated into the Council's final policy conclusions. The entire series was transmitted to the President and the Congress in May 1987.

The Council also commissioned several analyses of cross-cutting themes that emerged from earlier work. These included: the role of dedicated revenues and special districts in funding public works; the unique problems of small public works systems; the link between infrastructure and economic activity; how other nations view infrastructure in their economic development efforts; the adequacy of the nation's public works; and improving the performance of public works through better management and decision making.

The Council has found much that is good about what cities, counties, special districts, states, and the nation are doing in planning, building, operating, and maintaining America's infrastructure. But on balance, the Council concludes that our infrastructure is inadequate to sustain a stable and growing economy. As a nation, we need to renew our commitment to the future and make significant investments of our own to add to those of past generations.

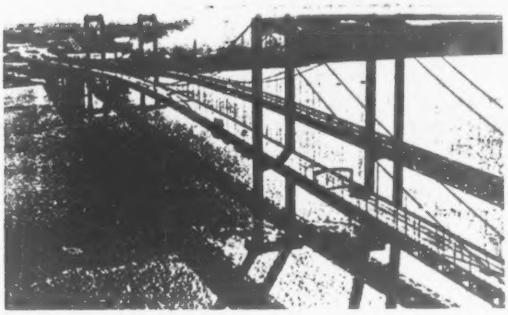
The Council and its staff are proud to report that the Council completed its work within its budget allocation and by the deadline established by the Congress.

Summary of Findings

The quality of a nation's infrastructure is a critical index of its economic vitality. Reliable transportation, clean water, and safe disposal of wastes are basic elements of civilized society and a productive economy. Their absence or failure introduces an intolerable dimension of risk and hardship to everyday life, and a major obstacle to growth and competitiveness.

The Erie Canal; the transcontinental railroads; the great dams and water systems of the west; the airports, seaports, and transit systems that serve our cities; our network of modern highways and soaring bridges—all these are part of this country's great public works inheritance from the generations of Americans who built before us. These massive and sometimes daring achievements supported the growth of the greatest economic power the world has ever known. They have been the envy of other countries and the model for our competitors.

Now that inheritance is in danger.



After two years of study, the National Council on Public Works Improvement (the "Council") has found convincing evidence that the quality of America's infrastructure is barely adequate to fulfill current requirements, and insufficient to meet the demands of future economic growth and development.

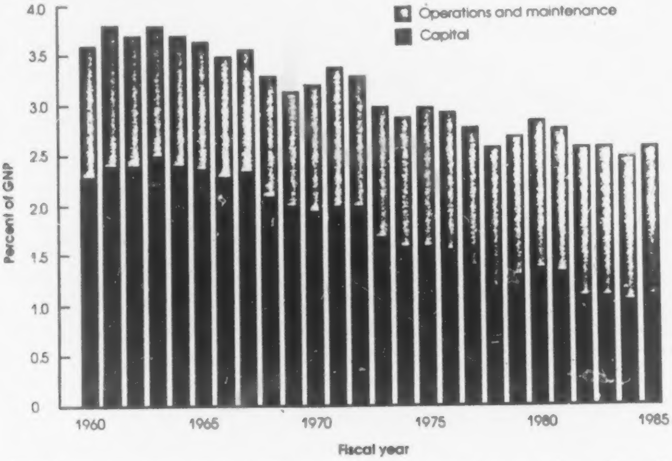
And unless we dramatically enhance the capacity and performance of the nation's public works, our own generation will forfeit its place in the American tradition of commitment to the future. Without such an effort, our legacy will be modest at best. At worst, we will default on our obligation to the future, and succeeding generations will have to compensate for our failures.

> *"We're spending our inheritance. You know, we built this freeway system . . . in the '50's and '60's, and we are still trying to make that do for today's needs."*
>
> Secretary Dewey Lonsberry,
> New Mexico Dept. of Highways
> and Transportation
> Council Hearing,
> Los Angeles, July 29, 1987

At present, most major categories of public works in the United States are performing at only passable levels. A few, such as water supply and water resources, remain in reasonably good shape. But others, such as solid waste and hazardous waste disposal, have serious and growing problems. In addition, smaller systems—in all categories and in nearly all regions of the country—face especially acute difficulties.

Part of the problem is financial. Overall investment in public works has slowed in the last two decades in relation to the demands of growth and environmental concerns. We have worn through the cushion of excess capacity built into earlier investments. In effect, we now are drawing down past investments without making commensurate investments of our own. Fig-

Figure 1—Public works outlays as a percent of GNP



Sources: U.S. Office of Management and Budget, *Budget Appendices of the United States*; U.S. Department of Commerce, Bureau of the Census, *Government Expenditure Series*; and *The Economic Report of the President*; for various years.

ure 1 illustrates this pattern of decline in public works spending as a percent of GNP.

With nearly one trillion dollars of public works assets[1] in the United States, reduced spending over the short term does not mean that individual facilities are in imminent danger of collapse, or that particular regions are in immediate peril. However, a declining infrastructure inevitably will jeopardize the productivity of our economy and our quality of life. Failure to reverse this decline will exact a high price for the nation in the future, both in the cost of deferred investment and in reduced economic competitiveness.

Therefore, the Council recommends a national commitment, shared by all levels of government, the private sector, and the public, to vastly improve America's infrastructure. Such a commitment could require an increase of up to 100 percent in the amount of capital the nation invests each year in new and existing public works. In 1985, this amount was approximately $45 billion.

Dramatically expanding current capacity or doubling the rate of capital spending is not an absolute requirement in all infrastructure categories at all levels of government, or in all regions of the country. However, an increase in capital spending of this magnitude is an important and achievable goal for the nation as a whole by the end of this century. For some categories, such as hazardous waste disposal, an even greater effort may be warranted.

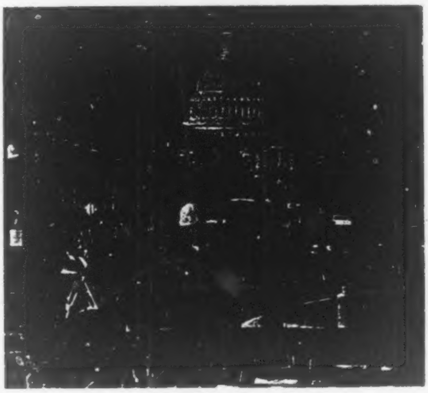
---

[1] This represents the approximate cumulative depreciated value of the public works facilities in the Council's purview. These include: highways, mass transit, aviation, water resources, water supply, and wastewater, solid waste and hazardous waste disposal. Public works can be interpreted more broadly to include communications, energy facilities, schools, hospitals, prisons, and parks. In an effort to target its resources, the Council has limited its primary focus to transportation, water, and waste disposal issues. Nevertheless, a considerable portion of its research findings and policy conclusions may apply to other areas.

A strategy to upgrade America's infrastructure must incorporate other tactics in addition to increased investment. **Thus the Council also recommends:**

- **Clarification of the respective roles of the federal, state and local governments in the construction and management of infrastructure to focus responsibility and increase accountability;**
- **Steps to improve the performance and efficiency of existing facilities;**
- **A rational capital budgeting process at all levels of government;**
- **Strong incentives to ensure adequate maintenance and, where appropriate, adopt new technologies; and**
- **More rigorous and widespread use of low capital techniques for delivering services and meeting service needs, such as demand management, coordinated land-use planning, and waste reduction and recycling.**

Through these measures the nation can make the best use of existing assets. This approach also may help to defer or avoid a significant portion of capital needs and costs that otherwise would be required in the future.

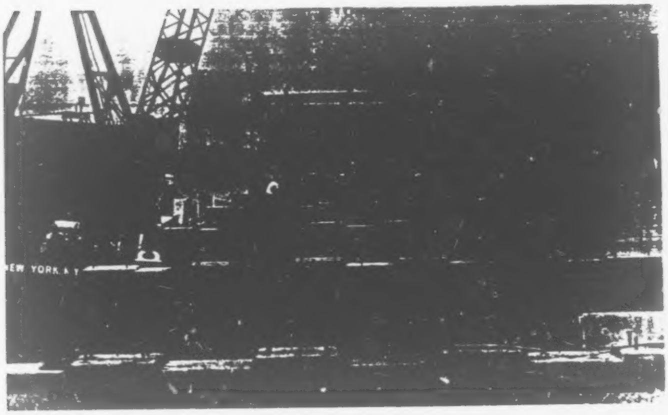


> *"Where in this myriad of problems is the good news? I would suggest that it lies in the opportunity to get government moving before an infrastructure crisis is upon us."*
>
> Michael Deland,
> Regional Administrator, EPA,
> Boston, Massachusetts
> Council Hearing,
> Boston, Aug. 3, 1987

The Council recommends that state and local governments continue to play their traditional leadership roles in the construction and management of the nation's infrastructure. But the Council also believes that the federal government must act as a full and responsible partner on a long-term basis in the national effort to increase and sustain public capital investment.

There is much to set right in America's house. The Council recognizes that an increased investment in infrastructure is just one among many critical claims on the nation's resources. To address this claim and others requires that we reckon first with the growing imbalance between consumption on the one hand and investment and savings on the other. This imbalance, reflected in the federal budget deficit and in other forms of borrowing against the future, affects all federal spending decisions. **The Council supports appropriate actions to redress the imbalance between consumption and savings so that future infrastructure commitments will not be shortchanged.**

The Council believes that infrastructure must rank high among our priorities. We must ensure that our highways and subways can move us swiftly and safely; that our homes, farms, and industries are supplied with ample clean water; that we re-



duce and safely dispose of the increasing volume of poisonous wastes our society generates; and that we provide the structural underpinning for a robust and competitive economy.

To reach this goal by the turn of the century, we must start now to rebuild what we have neglected, to repay where we have borrowed, and to invest again in our future and our children's future.

Joseph M. Giglio
Joseph M. Giglio
Chairman, New York, New York

Peter C Goldmark
Peter C. Goldmark Jr.
New York, New York

Lowell B. Jackson
Lowell Jackson
Aurora, Colorado

Freeman Holmer
Freeman Holmer
Eugene, Oregon

Frieda K. Walli
Frieda K. Wallison
Washington, D.C

Reinvesting in America

Sharply upgrading America's infrastructure is an ambitious goal. It cannot be achieved in a short period. Our infrastructure problems are manageable, but only if we begin to mobilize our resources now. These problems cannot and should not be solved through a crash program. Rather, success requires that all levels of government and the private sector dedicate themselves to a sustained effort.

This effort should focus on the effective capacity of our infrastructure systems—the level and quality of public services provided by each category. No single approach by itself will be adequate. More money alone will not suffice. More effective management alone will not get the job done. Technology will not save the day. The complexity of these systems and their attendant problems demand a broad-based strategy.

> *". . . there is no 'quick-fix' for the problem. It's much more likely to be solved—eventually—through deliberate remedial steps rather than through a fast, dramatic 'conversion' of practices and attitudes."*
>
> Mayor George Latimer,
> City of Saint Paul, Minnesota
> Letter to the Council,
> June 22, 1987

Rating America's Infrastructure Performance

To determine where we must go, we first must assess where we are. The current condition of the nation's infrastructure is hardly encouraging. If our public works were graded on an academic scale, their recent performance would earn a scant "C"—barely adequate to support current demands.

Yet a single grade cannot reflect the variability of performance by category or within categories. For example, municipal refuse is collected with some success, but limited landfill capacity is making disposal more expensive and less effective.

The report card on the following page provides an overview of the performance of eight categories of public works. By identifying recent program changes and outstanding policy concerns, it also highlights opportunities for improvement.

> *"The public needs to understand that major public works projects have a tremendous lead time, especially if they are located in a metropolitan area or involve controversy. It took more than 20 years from inception to the opening of Interstate 66 from the Capitol Beltway to the city of Washington, D.C."*
>
> Albert A. Grant, P.E., President,
> American Society of Civil Engineers

REPORT CARD ON THE NATION'S PUBLIC WORKS

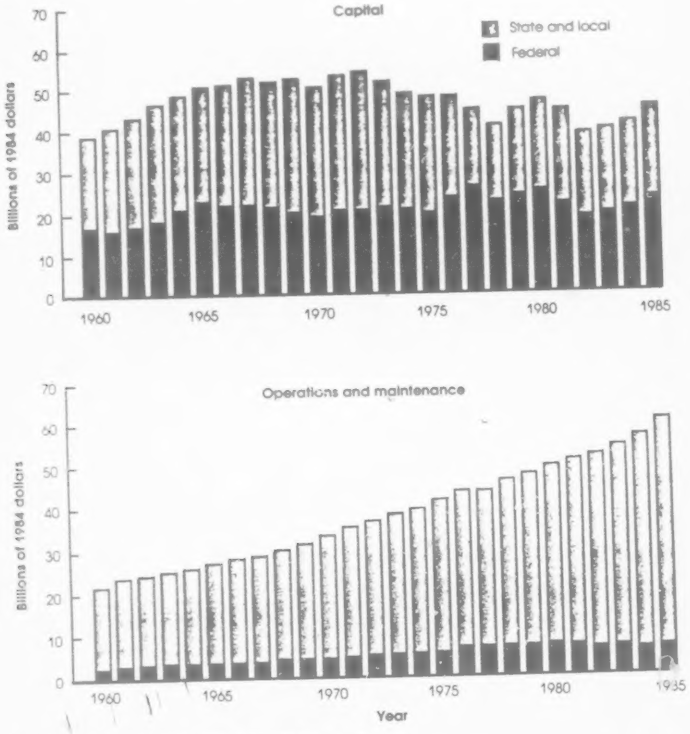
Subject Category	Grade	Successes/ Recent Changes	Problems/ Future Weaknesses
HIGHWAYS	C+	Federal and state gas tax increases have injected new capital into the system. This, along with inceased O&M spending, has improved pavement conditions. However, quality of service in terms of congestion is declining.	Spending for system expansion has fallen short of need in high-growth urban and suburban areas. Many roadways and bridges are aging and require major work. Needs of most rural and smaller systems exceed available resources. Highway Trust Fund has a sizeable cash balance.
MASS TRANSIT	C–	Federal capital grants have helped improve quality of service in some areas, but overall productivity of the system has declined significantly. Growth of transit vehicles is double the rate of increase in ridership. Diverting people from cars is increasingly difficult.	Mass transit is overcapitalized in many smaller cities and inadequate in large, older cities. Systems rarely are linked to land-use planning and broader transportation goals. Maintenance has been erratic and inadequate, especially in older cities.
AVIATION	B–	In general, the aviation system has handled rapid increases in demand safely and effectively. However, service has begun to decline in the face of increasing airport and airspace congestion as a result of strong traffic growth. The air traffic control system is currently undergoing a $16 bil... modernization.	Congestion is the system's primary problem. Despite recent increases in authorizations, sizeable cash balance remains unspent in the Airport and Airway Trust Fund. The air traffic control system needs substantial upgrading to maintain safety.
WATER RESOURCES	B	Water Resources Act of 1986 made cost-sharing mandatory for many types of water projects. This change should improve project selection and reduce overall project costs.	Cost-sharing will improve efficiency but also increase local costs of water projects. Poorer communities may find it difficult to finance projects. Implementation is often excessively slow and cumbersome.
WATER SUPPLY	B–	While regional performance varies, water supply stands out as an effective, locally-operated program. Strict new standards created by the 1986 Safe Drinking Water Act will require drastic increases in water rates over the next decade.	Many public water systems suffer from pricing below costs, inability to meet purity standards, or source contamination. Storage and distribution systems are deteriorating in some older cities and supplies are limited in some parts of the West and several cities along the East coast.
WASTEWATER	C	Over 75% of U.S. population is served by secondary treatment plants. Shift from federal grants to state revolving loans may improve efficiency of plant construction. Broadened focus on nonpoint source pollution and groundwater contamination may accelerate progress toward cleaner water.	Despite $44 billion federal investment in sewage treatment since 1972, water quality has not improved significantly. This is due in part to uncontrolled sources of pollution, such as run-off from farmland and roadways. Overall productivity of secondary treatment facilities is declining, resulting in an increase in water quality violations.
SOLID WASTE	C–	Testing and monitoring of solid waste facilities are more rigorous as a result of tougher environmental standards. Waste-to-energy technology is growing as alternative to landfills. More aggressive waste reduction, separation, and recycling efforts are beginning at the local level. However, few states have moved boldly on these measures.	Nation faces significant costs of adequate and safe facilities. Limited data suggest trends toward fewer but safer landfills, rapid growth in resource recovery, and little progress toward waste reduction. Public opposition to siting all types of facilities is a major problem.
HAZARDOUS WASTE	D	Funding for site clean-up has increased five-fold since 1986, but progress has been slower than expected. Only a small fraction of the two tons of waste per capita produced in America each year is being treated safely. Major challenge is still ahead of us.	Nation has forfeited much of its opportunity to reduce waste before it is produced. Waste control legislation promotes "end-of-pipe" rather than source reduction solutions. Congressional mandates and schedules may be overly optimistic, given administrative resources. A massive backlog of poisons and needed cleanup projects faces the nation.

Current Spending on Public Works[2]

Capital investment represents front-end, long-term resources committed to the plant and rolling stock that provide public works services. Measured in 1984 dollars, state and local capital investment peaked in 1972 at $34 billion; annual federal outlays for capital, however, peaked at $25 billion in the late 1970s. This trend is charted in Figure 2.

Spending for operations and maintenance (O&M) is key to the overall longevity and efficiency of public works capital assets. In the aggregate, spending for O&M has continued to grow at a rapid rate since the 1960s (from $21.6 billion in 1960 to $56.5

Figure 2—Government outlays for public works



Source: Apogee Research, Inc., Government expenditure databases.

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[2]All dollars are expressed in constant 1984 dollars, unless otherwise noted in the text.

billion in 1984), as also shown in Figure 2. Underlying this trend was a small decline in federal operating outlays since the mid-1970s and a substantial increase in local O&M outlays over the entire 24-year period.

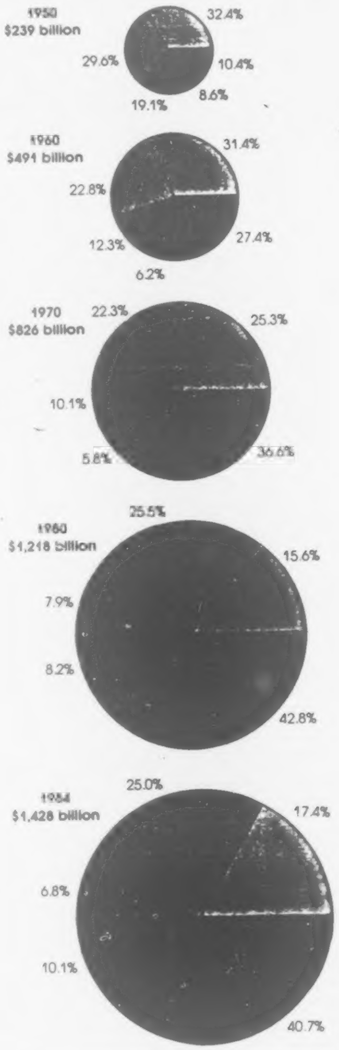
Public works spending patterns are of particular concern when viewed in relation to other measures of economic activity. For example, total public spending on infrastructure has dropped from 3.6 percent of the gross national product (GNP) in 1960 to 2.6 percent in 1985. While spending on operations and maintenance has remained a constant share of GNP, capital spending has dropped from 2.3 percent of GNP in 1960 to 1.1 percent today. The relative share of public works spending at all levels of government has declined drastically from nearly 20 percent of total expenditures in 1950 to less than 7 percent in 1984, as shown in Figure 3. During this same period, government spending for welfare and education increased from 10 percent to over 40 percent of total expenditures.

> *"There is . . . growing concern at the state and local level that . . . given competing demands for funding at the local level for education, health, welfare and public safety programs, the public works infrastructure may indeed experience severe deterioration in the coming years."*
>
> Harout Sanasarian, Supervisor
> Milwaukee County, Wisconsin
> Council Hearing,
> Indianapolis, July 12, 1987

Figure 3—All government spending, 1950-1984 in 1984 dollars

1950	$239 billion
1960	$491 billion
1970	$826 billion
1980	$1,218 billion
1984	$1,428 billion

- ▨ Defense
- ☐ Nondefense discretionary
- ■ Public works
- ■ Interest on general debt
- ■ Public welfare/education



Source: Apogee Research, Inc.

Public works investment is growing more slowly than private capital investment. Private-sector capital investment increased by about 51 percent between 1975 and 1985, but public works investment fell by more than 6 percent over the same period. Figure 4 shows the decline in public works spending per dollar of new private capital put in place.

Economic Prognosis

What do these trends mean for the health of the economy? The level of public works spending is only one indicator of the quantity and quality of service. However, we do know that public investment generally increases the productivity of private investment. Thus the growing imbalance between public and private investment means that we probably are not getting as much value as we could for every private investment dollar. The resulting loss in productivity limits the growth of the economy and our ability to compete in world markets.

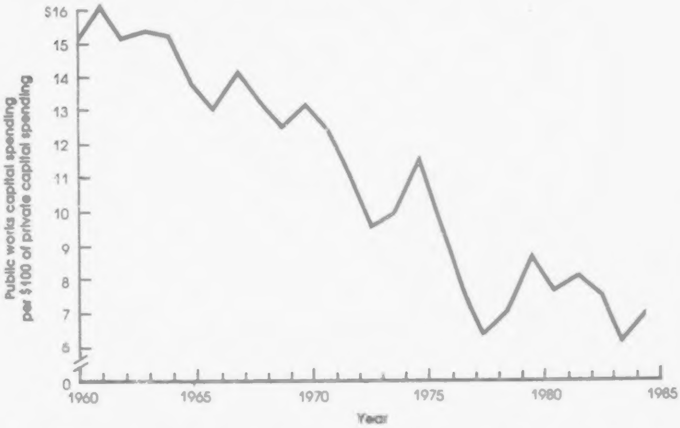
In light of these spending trends and the concerns about future performance outlined above, it is clear that substantially more must be done—and we must start soon.

> *"For the sake of our nation's future, we must provide the funds necessary to maintain and improve roadways and bridges. These are the networks essential for our economic survival."*
>
> James Sullivan, President,
> Greater Boston Chamber of Commerce
> Council Hearing,
> Boston, Aug. 3, 1987

Elected officials and the public at large must recognize that capital expenditures are not the only cost of public works; rather, the expense incurred through delays in providing needed services, added to the value of lost economic opportunities, often can exceed direct budget costs.

> *"The long pattern of disinvestment and a deteriorating infrastructure have eroded our capacities to sustain economic growth—growth which is translated directly into jobs for Americans."*
>
> The late
> Mayor Harold Washington
> City of Chicago
> Council Hearing,
> Chicago, Sept. 30, 1987

Figure 4—Comparison of public works capital spending to private capital spending



Sources: National Council on Public Works Improvement calculations based on the *Economic Report of the President*, January 1987, Appendix B, and Apogee Research, Inc., Government expenditures database

Our current level of capital investment is barely enough to offset annual depreciation, much less meet new demands. The U.S. Department of Commerce estimates that infrastructure use by industry alone will increase by at least 30 percent over the next ten years as a result of economic growth, the dispersion of population and economic activity, and technological and structural changes. Infrastructure capacity must keep pace with this increase while still maintaining the current quality of service. Better service—reduced congestion, improved water quality, higher safety levels—will require even greater capacity expansion, as well as extensive operational improvements.

> *"The condition of our transportation infrastructure is a critical factor in determining our nation's productivity and our ability to compete and survive in today's world market. We face widespread economic decline if we allow our tremendous highway infrastructure investment to deteriorate."*
>
> Commissioner Leonard Levine,
> Minnesota Department of
> Transportation
> Council Hearing,
> Chicago, Sept. 30, 1987

> *"Currently the cost of congestion in Los Angeles County is about 485,000 hours per day of wasted time by our residents or people driving through the county. That converts . . . by our estimates to a minimum of about $507 million per year in wasted time, and about 72 million gallons of gasoline . . . just in our county."*
>
> Rich Richmond, Executive Director,
> Los Angeles County
> Transportation Commission
> Council Hearing,
> Los Angeles, July 29, 1987

While a sound infrastructure does not guarantee future prosperity, long-term economic growth cannot be achieved without it. Economic efficiency and public health both are linked inextricably to adequate transportation, water quality, and waste disposal services. In addition, infrastructure investment directly supports additional economic activity. For every public dollar spent on an annual basis to build and maintain our network of roads, streets, and bridges, the private sector spends $15 to move people and goods. For every public aviation dollar, private firms and individuals spend nine.

If we spend too little on public works or if we invest in inefficient projects, society loses more than the direct public cost. In the long run, our ability to compete in the international economy will be weakened, and our standard of living will suffer.

Finding the Money

Much of the discussion about public works in recent years has focused on choosing appropriate finance mechanisms—e.g., revolving loan funds, intergovernmental grants, tax-exempt debt techniques, or various forms of privatization. While these options may differ in terms of the attractions they offer to public officials, they all draw on two basic sources of funds—*general tax revenues* and *user fees*.

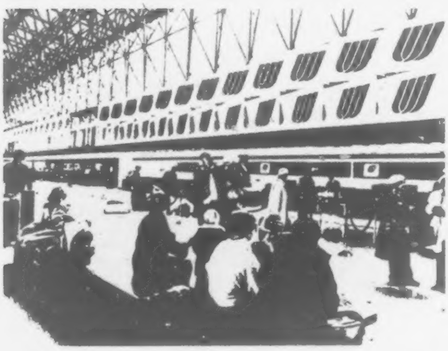
Mobilizing adequate financing to meet our current and future public works needs requires participation by all levels of government. **The Council endorses the following principles to guide this effort:**

- **Users and other beneficiaries should pay a greater share of the cost of infrastructure service.**
- **The federal government should be a reliable partner in financing public works.**
- **States should develop comprehensive infrastructure finance strategies.**
- **Local governments should give budgetary priority to funding the maintenance of existing facilities.**

Emphasis on the Beneficiaries

Today almost 75 percent of public capital spending on infrastructure is derived from users. Yet only about 50 percent of spending on operations and maintenance comes from this source. Significant elements of transportation, water supply, wastewater treatment, and solid and hazardous waste systems serve identifiable consumers on a continuing basis. Use can be measured and priced; those who do not pay can be excluded from services. Linking financing to use can produce a steady and predictable revenue stream, encouraging better maintenance, rehabilitation, and replacement.

> *"New strategies like public-private partnerships will help. So will federal initiatives.... But what I think is really needed first is a national consensus. We need to better define the scope of the problem—what are the specific needs for all levels—and then identify what resources can be marshalled and by whom."*
>
> Mayor Don Erickson,
> Cheyenne, Wyoming
> Council Hearing,
> Los Angeles, July 29, 1987



The Council recognizes important limitations to the user fee principle. Many smaller communities lack the financial base necessary to finance a facility—especially when new capital investment is required. Fees for certain types of essential services, such as water supply, sewage treatment, and solid waste disposal, also can be excessively expensive for lower income residents or hard-to-serve areas.

Options to address these problems may include guarantees or insurance for small-issue debt; state bond banks that combine small bond issues into larger, more creditworthy statewide issues; selected increases in grants targeted to smaller facilities or those serving lower income areas; and re-gionalization of services to achieve economies of scale. Providing a threshold level of service and a safety net in these instances also may require general revenues to supplement user fees.

Public works produce both direct and indirect benefits. For example, a mass transit system benefits the transit riders as well as the motorists who travel in the area. In addition, mass transit often benefits business and commercial interests. Thus, the cost of transit development or expansion should be borne by all three groups.

> *"Twenty years ago developers looked almost entirely to the public sector for infrastructure. Today with increasing population and migration of people and businesses to the cities and surrounding counties of Nashville growing so much faster, the public sector can no longer provide total infrastructure needs. The future must be a joint effort."*
>
> George Volkert, President,
> Southeast Venture Company,
> Nashville, Tenn.
> Council Hearing, Nashville, June 9, 1986

User fees may prove inadequate for major new investments in infrastructure technology and economic development. Such projects have few immediate or easily identifiable beneficiaries. Instead, they represent long-term commitments to the future, and rightfully are a matter of common responsibility, to be financed out of general funds or a user fee base that includes both present and future beneficiaries.

The Council endorses the general principle that developers should pay an equitable portion of the cost of new facilities necessary to service commercial, industrial, and residential development. State and local officials should exercise due care to see that the allocation of such costs is fair and reasonable and does not result in undue private influence over public development policies and priorities. Further, it should be recognized that developer fees and exactions will have an impact on the cost and availabilty of housing.

The Council urges that federal user fees paid in good faith by beneficiaries to preserve and protect public works systems be spent for that purpose. The accumulation of unspent balances in the federal highway, transit, aviation, and waterways trust funds—nearly $24 billion in the 1987 budget—is at odds with this principle. **The Council supports a determined, incremental effort to reduce these balances—in line with responsible management and planning—so that the funds can be used for necessary infrastructure improvements.**

Federal Partnership

Between 1960 and 1975, federal grants-in-aid as a portion of total state and local capital spending remained relatively stable at about 33 percent (Figure 5). In the late 1970s, federal aid rose to more than 50 percent; since then it has leveled off at 40 to 45 percent. These patterns reflect a decline in capital spending by state and local governments as well as shifts in federal grant policy.

In the realm of infrastructure finance, the federal government traditionally has focused on providing public works capital. Because of its limited involvement in maintenance and operations, the federal government accounts for less than 30 percent of all public works spending.

The Council urges the President and the Congress to recognize the importance of maintaining a continuing federal role in infrastructure finance. Intergovernmental aid still is necessary to launch major projects of national interest, or to help governments with limited fiscal capacity. However, some changes in the form of federal spending may be necessary to accommodate shifting federal, state, and local roles and relative fiscal capacities.

Whatever form federal assistance takes, it should offer state and local governments:

- Stability over several years to aid long-range planning;
- Flexibility in the use of funds through such mechanisms as block grants; and
- Incentives for increased efficiency and improved maintenance.

In addition, the federal government should exercise restraint in adopting legislation that would limit the revenue-raising capacities of state and local governments.

> *"I think we have seen the end of . . . massive amounts of federal dollars returning to local governments through federal revenue sharing and any grant program. I think at the state and local levels we must . . . go to Washington and ask for programs and policies that are feasible in light of the changed fiscal circumstances."*
>
> Ronald Bean, Executive Director,
> Illinois Development Finance Authority
> Council Hearing,
> Chicago, Sept. 30, 1987

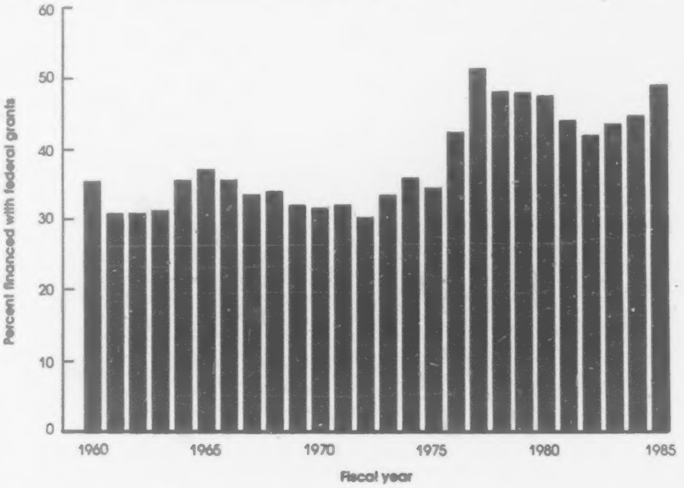
Federal tax policy also has a significant impact on infrastructure finance. For example, the Tax Reform Act of 1986 drastically limits arbitrage earnings on borrowed funds and restricts the use of municipal bond proceeds for quasi-public projects by imposing ceilings on allowable issues. These and other provisions are expected to limit the growth of tax-exempt bonds, and to increase state and local borrowing costs. The law also lengthens depreciation schedules and repeals investment tax credits, which will increase the cost of joint development of certain public works with the private sector. In combination, the provisions of the 1986 law may impede the financial plans of state and local governments, reduce their fiscal capacity, and limit their ability to finance necessary improvements.

The Council urges the President and the Congress to pay close attention to the effects of tax reform, and to remove unwarranted limitations on the power of state and local governments to finance public works.

State Strategies

Although a number of states have instituted innovative financing programs, the state share of overall spending on infrastructure dropped from 32 percent in 1970 to 23 percent in 1985. At $25 billion annually, state

Figure 5—Percent of state and local public works capital spending financed with federal grants



Source: Apogee Research, Inc., Government expenditures databases.

taxes and fees now finance less than one-third of expenditures on state and local public works programs.

While localities are under pressure to fund an increasing portion of total public works spending, often they must contend with state restrictions on taxation or bonding. For example, as of 1985, 31 states had imposed specific property tax rate limits on local governments. Six states had either constitutional or statutory limits on the total amount of revenues that local governments could collect annually.

The Council encourages governors and state legislatures to examine the impact of such restrictions on state and local public works. Where state constitutional or statutory limitations hinder the ability of the state and local jurisdictions to deliver essential services or adversely affect their credit ratings and finance capacity, states should assume responsibility for either remedying the situation or providing compensatory assistance.

"We as local communities are property tax dependent. We have no access . . . and it is true in most all New England states, to any other forms of taxation."

Pam Plumb, City Council
Member, Portland, Maine,
and 1988 President of the
National League of Cities
Council Hearing,
Boston, Aug. 4, 1987

Future Finance Options

The Council has called for a substantial increase in the capacity and effectiveness of the nation's public works. This goal is not attainable unless we first make better use of existing financial resources. In most cases, however, we cannot rely simply on wiser spending; we also must generate additional sources of funding. This burden will fall on all levels of government and involve virtually every category of public works.

The Council supports the concept that the unit of government responsible for service delivery should be the one that levies the fees or taxes to the extent possible and practical. This will strengthen accountability for the cost and quality of public works service. Local governments already bear the lion's share of operating and maintenance costs and a growing portion of capital costs as well. But to carry out their responsibilities, they must have the proper tools, such as taxing and bonding authority and access to the tax-exempt municipal bond market.

"One point seems to be very clear. The people are willing to dig into their own pockets to pay for better roads, more schools, clean water, expanded airports, improved transportation, and the items which help shape the quality of life in the Golden State."

Don McGrew, President,
Griffith Company,
Long Beach, California
Council Hearing,
Los Angeles, July 29, 1987

It is not appropriate for the Council to propose a specific legislative program of new fees and taxes to finance public works improvements. The most equitable and efficient mechanisms will depend on the type of infrastructure problem being addressed and on local conditions, traditions, and institutions. These trade-offs are made through the political process at all levels of government. The menu of possible revenue sources listed in Table 1 provides a starting point for assembling such a program.

Many of the options in Table 1 represent simple expansions of existing user fees or related excise taxes. The largest potential sources of funding are motor fuel taxes used by the federal and state governments to support highways and some transit spending, and developer exactions and related fees imposed by many local governments. Local exactions are perhaps the fastest growing means of infrastructure finance, as well as the least well known.

Table 1.—Possible Sources of New Public Works Revenues

Source	Level of Government	Current Rate	Possible Increment	Potential Revenues ($ millions/year)
Motor Fuels Tax				
a) Flat Tax	F,S,L	$0.23/gal[a]	$0.10/gal	$12,000
b) Ad Valorem	F,S,L	(b)	10% of fuel costs	9,500
Repeal Exemptions from Highway Taxes	F	(c)	N.A.	1,000
Heavy Truck Taxes	F,S			1,000
Aviation Ticket Tax	F	8% of value	2% of value	800
Airport Service Charge	L	None[d]	$3/passenger	1,500
Inland Barge Fuel	F	$0.10/gal[e]	$0.10/gal	50
Port Tax	F	0.04% of cargo value	0.06% of cargo value	250
Cash Balances in Trust Fund Cash	F	N.A.	(f)	2,000
Water Supply	F,S	None[g]	$0.10/1,000 gallons	750
Waste-End Taxes	F,S			
a) Generation		None	$5/ton	1,500
b) Disposal —by Hazard		None	$0-$60/ton	2,600
c) Disposal —by Method		None	$4-$25/ton	3,200
Local Impact Fees on Developers	L	(h)	(i)	10,000-15,000

NOTE: Revenue estimates show gross receipts and have not been adjusted for potential reductions in other taxes. These offsets could reduce gross receipts by as much as 25 percent.

SOURCE: Apogee Research

[a] The current federal tax is 9 cents per gallon of gasoline. State taxes average 14 cents per gallon. The federal government taxes diesel fuel at an additional 6 cents per gallon.

[b] Some states currently collect sales taxes on motor fuel.

[c] State and local vehicles, transit buses and users of gasohol are exempt from certain federal and state taxes despite the wear and tear they cause on roads and bridges.

[d] This charge, commonly referred to as a "head tax," currently is prohibited by federal law.

[e] Scheduled to increase to 20 cents per gallon by 1995.

[f] Assumes the current trust fund cash balances will be used over the next ten years.

[g] None at the federal level; Washington is one of the few states with a water excise tax.

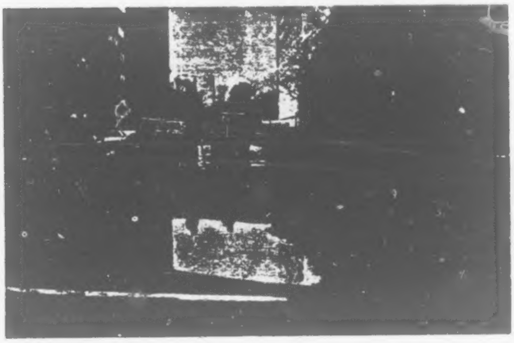
[h] Many local governments already impose some form of negotiated fee for the infrastructure costs resulting from new development.

[i] Assumes that impact fees and related techniques are increased to equal 20 to 30 percent of capital spending. Potential revenues are not likely to be realized until the mid-1990s.

Sharpening Accountability for Infrastructure

Dependable, high-quality infrastructure is not the product of money alone; building and maintaining public works requires a shared vision, commitment of time and energy, and the skills of people throughout the public and private sectors. Historically, such consensus often has been a local or regional phenomenon in America. The result is a system that is highly decentralized and subject to continual change. Each community has its own laws, traditions, and other characteristics that govern the way it apportions responsibility and resources for public works.

On the whole, this system has worked well in providing public works facilities and services for a large number of communities. But too often, when problems arise, ultimate responsibility among various levels of government is not understood clearly by either the public or its leaders. When the solutions are costly, complex, and controversial, or involve a wide range of players, our tendency, as individual communities and as a nation, is to stall and point our fingers at the "other guy" until we reach a crisis. By this time we generally have foregone the most sensible and inexpensive options. Last summer's story of the Long Island garbage barge wandering forlornly around the Caribbean is one such example. Most of its cargo was used paper—a commodity that could have been recycled for sale in many parts of the world. In the end, accountability was fixed back on the community that generated the garbage, but by then the cargo was waterlogged and without value.



The Council urges that the roles of the federal, state, and local governments be clarified to help boost the performance of the nation's public works.

In general, the Council believes the federal government should continue its primary role in hazardous waste disposal and clean-up, air traffic control, inland waterways, highways of national significance, intermodal freight transportation, minimum performance standards for environmental protection, major capital investments for flood control and shoreline protection, and the overall coordination of water resource programs.

> *"There is no perfect solution to solid waste disposal. . . . Everything we do will have some minor impact. . . . It must be disposed of and that place is inevitably in somebody else's backyard, and that is one of our problems."*
>
> Frank Borchardt,
> Executive Vice President,
> HDR Techserv,
> Omaha, Nebraska
> Council Hearing,
> Chicago, Sept. 30, 1987

In turn, states should have lead responsibility for highways of statewide significance, non-federal dam safety, major capital financing of wastewater treatment, airport system planning, and the siting of waste disposal facilities.

Local governments, or in some cases regional authorities, should have primary responsibility for local streets and roads, public transit, individual airports, water supply systems, ports, urban stormwater, wastewater treatment facilities, and solid waste disposal. In many instances, these services may be financed and operated by private firms through agreements with local jurisdictions. Opportunities for private participation should be considered actively by all levels of government but should not be seen as a panacea.

The impact and importance of most public works are not neatly locked within the boundaries of any given jurisdiction. One community's failure to provide good roads or adequate sewage treatment may hinder all others in the vicinity. Stewardship of the infrastructure as a whole demands some degree of accountability by all levels of government. However, in a dynamic and fractionated federal system such as ours, accountability can be measured more usefully against general principles than rigid standards.

The Council believes that state and federal infrastructure policy should support local self-sufficiency to the greatest extent possible. This means that:

(1) **Federal and state statutes should be far clearer and more rigorous in specifying who is responsible for doing what, and by what deadline.** Many laws and program guidelines governing complex projects contribute to delay and lack of accountability by failing to set timely deadlines for reviews. Nor do they specify who will resolve conflicting advice or opinions when many different agencies are involved. The immense difficulties of siting solid and hazardous waste facilities and the long, costly delays associated with port and navigation projects are reflections of this bureaucratic equivocation;

(2) **Federal and state public works mandates should be considered carefully and allow cost-effective methods of compliance rather than rigid technical requirements.** For example, in older urban areas, "dial-a-ride" services can provide equivalent mobility for the physically handicapped more cost-effectively than retrofitting all transit vehicles;

(3) **Rules governing state and federal programs should recognize the distinct financial and managerial needs of small and rural governments;**

(4) **States should seek to promote cooperation among local jurisdictions, as well as between state and local government.** State advisory councils on intergovernmental relations, regional planning commissions, councils of government, and interlocal agreements are useful mechanisms to achieve this goal; and

(5) **The federal and state governments should address the need for adequate technical information and expertise when they impose responsibilities on local government.** "Circuit riders" or other forms of technical assistance and training should be considered where appropriate.

Strengthening System Performance

The principal value of public works lies in the services they deliver—e.g., reliable transportation, clean water, and safe disposal of wastes. Physical assets, such as pipes, bridges, and lane-miles of freeway, make these services possible, but they come with no guarantee that they will deliver the quality, quantity, or cost of service needed to sustain our economy and standard of living. The performance of these assets depends on a range of human and technical factors, as well as the ongoing level of capital investment and maintenance.

If, as the Council recommends, the public is asked to provide increased capital for current and future infrastructure capacity, governments at all levels have a corresponding responsibility to get the maximum value out of every dollar spent. In many cases, it may be possible and prudent to postpone some new investment by increasing efficiency through improved operations, employing more aggressive maintenance procedures, and adopting various demand management techniques (such as full-cost pricing, land-use policies, or waste reduction and recycling).

Public works design, construction, operation, and maintenance should be viewed as phases of a single process. New equipment or facilities can be designed and built for ease of operation and maintenance. Timely repairs reduce long-term operating costs and ensure the full life expectancy of existing facilities and equipment. Innovative operations sometimes can add capacity for little cost and reduce maintenance needs (e.g., computerized traffic control systems and non-corrosive snow and ice melting compounds).

The Council encourages renewed attention at every level of government to maintaining our current assets to optimum standards. Maintenance is perhaps the single most important element of governments' stewardship obligation. It also is the element that is easiest to defer, and the one most likely to be cut from the current expense budget.

Maintenance must be made more visible. This means providing understandable information on infrastructure conditions, performance, maintenance costs, and the annual amounts of deferred maintenance.

> *"When highways and bridges are regularly maintained there is no press coverage. When they are rebuilt it is an 'event.' There is a ribbon-cutting and plenty of press coverage. The incentives, therefore, are for public officials to purposefully starve the maintenance budget. . . . Until this motivation . . . is acted upon, we will be treated to recurrent infrastructure crises. In fact, proposals for infrastructure bonds, banks, etc., only abet this whole process."*
>
> Edward V. Regan, State Comptroller,
> State of New York
> Letter to the Council, January 15, 1988

It means actively educating the public—as shareholders in the nation's capital stock—to the importance of the *long-term* integrity of the system. In fact, public education is an important element of any strategy to improve our nation's infrastructure.

> *"One of the problems with the streets is that as you delay, the cost escalates. . . . If you allow them to fail without maintenance, then you are tripling or quadrupling . . . the cost to repair a street versus just maintaining it."*
>
> Robert Horii, City Engineer,
> Los Angeles Dept. of Public Works
> Council Hearing,
> Los Angeles, July 29, 1987

Other options that may help to lengthen the life of infrastructure systems include removing restrictions on federal and state grant funds to allow them to be used for improved operations and maintenance, and creating stronger maintenance incentives in revenue bond covenants.

The Council endorses a variety of operational improvements to increase current capacity and improve performance. For example, the primary problem with airport and airway facilities is congestion. However, new runways may not be the only answer; the solution at some airports may be to install available equipment that allows planes to depart and land safely at closer intervals. Demand management strategies, such as peak load landing fees, have reduced congestion at all three major airports serving the New York/New Jersey metropolitan area.

Demand for waste disposal facilities can be managed by waste reduction, separation, and recycling. Certain states have established goals of recycling anywhere from 15 to 40 percent of the waste stream. For example, ten states, including Oregon, Massachusetts, Maine, and Michigan, have implemented "bottle bills" to promote recycling and reduce waste. Massachusetts also is constructing a number of materials recovery facilities throughout the state.

Regulations governing product packaging can help reduce waste. Fees or surcharges on items that are difficult to dispose of (e.g., lead, zinc, or plastics) can reduce their use. Regulations requiring reuse of, or deposits on, recyclable items such as automotive batteries and motor oil serve the same purpose.

The Council strongly encourages all levels of government to upgrade the quality and quantity of basic public works management information in order to measure and improve system performance. At present, too many infrastructure investment decisions in America are made "by the seat of the pants." Small and medium-sized jurisdictions (and many large ones too) do not have complete inventories of existing facilities; most do not conduct regular surveys of the condition of public facilities or collect information on the quality, quantity, or cost of services. Only a handful of jurisdictions take advantage of established analytic techniques for computer mapping, life-cycle cost analysis, automated asset management, or precise tracking of growth trends.

While the up-front costs and paperwork required to set up data collection, management, and reporting systems can appear formidable, the absence of this information means that public officials must make multi-million dollar investment decisions on an *ad hoc* basis. The costs of estimating required capacity incorrectly or selecting a project ill-suited to needs can be staggering, particularly in the face of the fiscal and economic pressures facing most state and local governments.

In planning for public works investments, every jurisdiction should be guided by clearly stated performance objectives, consider alternative ways of achieving them, and have access to realistic information about costs of operation and maintenance. The capital budgeting process should

examine the entire range of public works needs to guarantee that the choices made reflect a rational set of priorities.

> *"Only with broad public understanding and support, especially as perceived by the responsible public officials, can any initiative or action involving political risk be successful."*
>
> Walter T. Olson, Program Director,
> Build-up Greater Cleveland
> Council Hearing, Chicago, Sept. 30, 1987

> *In Madison, Wisconsin, a $40,000 public education campaign convinced many residents to shift their water use away from the 6 p.m. peak. The relatively modest investment averted the construction of a new well system once thought necessary to meet peak demands. Savings to the community were at least $750,000 in new well construction, plus some $60,000 a year in operating costs.*

The private sector and a majority of state and local governments are setting the course and establishing proper standards for capital budgeting to meet generally accepted accounting principles (GAAP) and to gain a clearer picture of their capital needs and related financing requirements and resources.

The Council believes that the federal government should consider following their example. Capital budgeting at the federal level should seek to identify, define, and present separate operating and capital components of the federal budget while *maintaining a unified budget*. Direct federal spending on capital projects—such as roads and bridges, hospitals and housing, and military bases—and federal grants to state and local governments represent distinct forms of federal capital investment that may require different approaches. However, both can benefit from better planning and more consistent allocation procedures.

By requiring an annual analysis of federal capital spending, the Federal Capital Investment Program Information Act of 1984 (passed as Title II of P.L. 98-501 which established the Council) provided a constructive first step toward the development of an overall federal infrastructure strategy. **The Council urges the Congress and the President to institute capital planning and budgeting procedures as an integral element of the federal decision-making process. Such procedures would be the next logical step toward building a stronger fiscal—and physical—foundation for America.**

The City of Saint Paul offers one example of a far-reaching program designed to take advantage of computer technology and avert future crises. The first phase, Computerized Infrastructure Inventory, *was put in place in 1986, and provides a detailed data-base on the construction materials, location, age, and condition of all the city's public works facilities. The second phase,* Computerized Maintenance Management, *which began to be implemented this past summer, links inventory data to city maintenance schedules, requests for service, and maintenance results. The third phase,* Computerized Mapping, *will be installed in the next few years and is expected to provide a complete electronic map of all streets in Saint Paul. Public works managers will be able to "overlay" infrastructure information on this map in order to develop and analyze maintenance strategies.*

Accelerating Innovation

The strength of America's infrastructure systems directly reflects our capacity and commitment to renew and improve public works technologies and their applications. Such technologies range from sophisticated robotics for trenchless pipe-laying to the asphalt used to pave the streets. Their development, implementation, and maintenance depend on a combination of knowledge, materials, equipment, and skilled people. Innovative, up-to-date technologies can guarantee efficient, safe, effective service and contribute to economic growth. Outdated technologies may endanger public safety, increase the cost of service, and reduce the competitiveness of business and industry.

The Council finds that the level of effort and resources applied to infrastructure research and development (R&D) in the United States falls far short of current as well as future requirements. Federal spending on infrastructure R&D in 1985 was approximately $103 million, less than one third of one percent of total new infrastructure construction in that same year. This portion has been falling steadily in recent years, as has private sector spending on similar activities. The potential return on more research is enormous.

Such a decline in R&D is especially troubling in light of evidence that the nation is becoming more dependent on foreign producers in certain public works categories. For instance, not a single American-owned firm currently builds transit rail cars. U.S. imports of machinery exceeded exports by $15.8 billion, or 27 percent, in 1985. By comparison, only a decade ago, our machinery exports exceeded imports by 58 percent.

> *"We have lost a generation of talent in transportation . . . because we haven't been putting money to support R&D through universities."*
>
> Dr. Robert Paaswell, Executive Director,
> Chicago Transit Authority
> Council Hearing,
> Chicago, Sept. 30, 1987

Other developed countries give greater support to public works R&D and technical innovation. Most of our trading partners invest a larger share of GNP in infrastructure R&D than the U.S. In addition, Japan and many European governments support R&D through tax incentives or matching funds, as well as flexible bidding and contracting arrangements. Major Japanese construction firms, although they had less than two-thirds the contract volume of their American counterparts, spent ten times as much on R&D in 1985. A sustained investment of this magnitude is likely to produce an increasing number of "cutting-edge" technologies that will find their way into the American public works construction market.

With nearly a trillion dollars of infrastructure fixed assets already in place in the United States, small changes in the reliability or efficiency of key components can result in major cost savings. However, we also face emerging problems of immense technical complexity—such as groundwater contamination, hazardous waste disposal, and traffic and airport congestion—that demand much more than tinkering with current methods. Technology is not the total answer, but clearly it is an essential part of it.

"Science and technology are fundamental to U.S. competitiveness. America's preeminence in research and innovation has long been the envy of the world and a critical source of our national strength."

President Ronald Reagan
State of the Union Message,
1987

Currently, no federal agency or other organization has the primary responsibility for systematically focusing national R&D efforts on infrastructure problems. Current federal programs are spread over a number of agencies with narrowly targeted missions. Ongoing research efforts conducted by other levels of government, professional organizations, and the private sector are fragmented and aimed only at incremental improvements. The opportunities for major breakthroughs and for sharing research results among all groups often are very limited.

The Council concludes that the scope and complexity of infrastructure problems throughout the United States merit a far more intense national focus on public works technology. This focus should be comprehensive—encompassing all infrastructure categories. It should be cooperative—involving representatives of all levels of government, professional organizations, and the private sector. Finally, it should be coordinated—tying together and building upon current R&D efforts.

While federal leadership and a continuing national framework are necessary, this approach need not require a large new federal bureaucracy. The Council believes that the goal of accelerating public works innovation would be served best by regional centers responsive to the public works market and particular variations and requirements within their respective geographic areas. Such centers could be either university based or operated in conjunction with existing research institutions.

Models for this approach are readily available. The National Science Foundation recently established specialized Engineering Research Centers at a number of universities. Each is focusing on a major topic of interest in engineering—for example, systems engineering for large structures at Lehigh University—with the aim of developing a center of excellence in its field. The Department of Transportation is in the process of creating ten regional university-based centers for R&D.

The Council also recognizes that the significant technical, financial, and legal risks involved with innovation can deter development and application. Risk-sharing arrangements for demonstration projects that test technology in an operating environment can help overcome these barriers. The size of many projects and the degree of risk involved may require a federal role. The federal government has assumed such responsibility in the past—most notably in the field of energy development—and the extent of our infrastructure needs may justify its doing so again.

Funding for efforts to expand infrastructure innovation should be provided by all levels of government and the private sector, with additional support from consumers as well. The latter could be collected in the form of a small assessment on utility bills earmarked for research and development in areas related to the source of funds. For instance, a 10 cent monthly assessment on year-round housing served by public sewers would yield over $77 million a year. A small percentage of public infrastructure capital funds also could be set aside for R&D. Potential sources include dedicated revenues, grants, trust funds, and general revenue contributions to capital budgets.

The Council also recognizes that to encourage and implement innovative technology, we must provide adequate education and training for the people who build, manage, and operate public works. These tasks demand increasingly complex technical and professional competencies, particularly in the areas of maintenance and rehabilitation.

Enrollments in schools of civil engineering—traditionally the mainstay of the public works profession—are declining significantly just as many senior engineers are reaching retirement age. Over the period 1985-1989, about 16 percent of all engineers in state transportation agencies are expected to retire; in some states the figure will exceed 20 percent. Yet between 1984 and 1987, the number of bachelor degrees awarded in engineering declined from 76,931 to 71,372. The share of degrees awarded in civil engineering has been falling rapidly: from about 20.3 percent in 1976 to 15.7 percent in 1982, and then to 12.8 percent in 1984. In addition, civil engineering graduates often have more financially rewarding job opportunities than are available in public works agencies.

The Council concludes that the nation has a shortage of technically competent personnel to meet future requirements of the public works profession. Federal action is needed to support and stimulate the education and training of public works professionals from all disciplines and academic specialties. Government agencies and private organizations should conduct an aggressive and sustained campaign to encourage young people to enter the profession. Major professional organizations such as the American Public Works Association and the American Society of Civil Engineers already have taken the initiative on this issue.

"There should be an immediate national concern for the provision of public works management training for the next generation of leaders in this field."

Max Whitman, Director of Public
Works, Village of Winnetka, Illinois
Council Hearing,
Chicago, Sept. 30, 1987

However, they should receive much more active support from government, business, and the education community. In addition, specialists from a range of other fields who could apply fresh perspectives should be encouraged to join the public works profession. Finally, retraining and continuing education programs should be utilized to upgrade the skills and abilities of current staff members.

A Strategy for Improving America's Public Works

No single approach is adequate to ensure the future viability of America's infrastructure. A broad range of measures is necessary to make a meaningful difference by the turn of the century. Specifically, these should include:

- **A national commitment, shared by all levels of government and the private sector, to increase capital spending by as much as 100 percent above current levels;**
- **Clarification of the respective roles of the federal, state, and local governments in infrastructure construction and management to focus responsibility and increase accountability;**
- **More flexible administration of federal and state mandates to allow cost-effective methods of compliance;**
- **Accelerated spending of the federal highway, transit, aviation, and waterways trust funds;**
- **Financing of a larger share of the cost of public works by those who benefit from services;**
- **Removal of unwarranted limits on the ability of state and local governments to help themselves through tax-exempt financing;**
- **Strong incentives for maintenance of capital assets and the use of low-capital techniques such as demand management, coordinated land-use planning, and waste reduction and recycling;**
- **Additional support for research and development to accelerate technological innovation and for training of public works professionals; and**
- **A rational capital budgeting process at all levels of government.**

None of these steps will be easy or unopposed. But the increasing cost of delay is certain. The Council urges the President, the Congress, and the nation's state and local leaders to act on this agenda immediately.

Acknowledgments

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GOOD NEWS ABOUT INFRASTRUCTURE

Sure, our bridges, sewers, airports, and roads are overaged and overused. But better management and financing can turn the crisis into just one more ordinary problem.

■ *by Nancy J. Perry*

TO READ the headlines, America the Beautiful has turned into a beast: TEN OR MORE MAY BE DEAD IN BRIDGE FALL. AMERICA IS BUCKLING AND LEAKING. GARBAGE BARGE EARTH. GRIDLOCK! In December, New York City tabloids ran wild with the story of a 28-year-old Brooklyn woman who was critically injured when she fell through a weakened sidewalk grate and landed on subway tracks 50 feet below.

Pretty scary stuff. But do the disaster stories accurately reflect the condition of the tangled network of American highways, subways, airports, sewers, reservoirs, and landfills that is felicitously known as infrastructure? Interviews with scores of politicians, public works engineers, and businessmen suggest that the answer is no. True, the infrastructure is aging and, as the population increases, new demands are placed on it. But more and more local governments have turned the infrastructure "crisis" into just another problem. Their secret: better management techniques to make facilities and financing go further. Let's call it nfrastretching.

Corporations and ommunities know the alue of good infrastruc-ure. In a 1988 Lou Har-is survey of 250 com-anies conducted for ushman & Wakefield, a eal estate firm, most re-pondents rated "easy ccess to domestic mar-ets, customers, or clients" as the most important factor in choosing an office location. The survey ranked Atlanta, which boasts an impressive array of freeways, mass transit, and air transportation facilities, as the No. 1 city in which to put a business. Says George Berry, Georgia Commissioner of Industry and Trade: "Transportation services are to Atlanta what gambling is to Las Vegas."

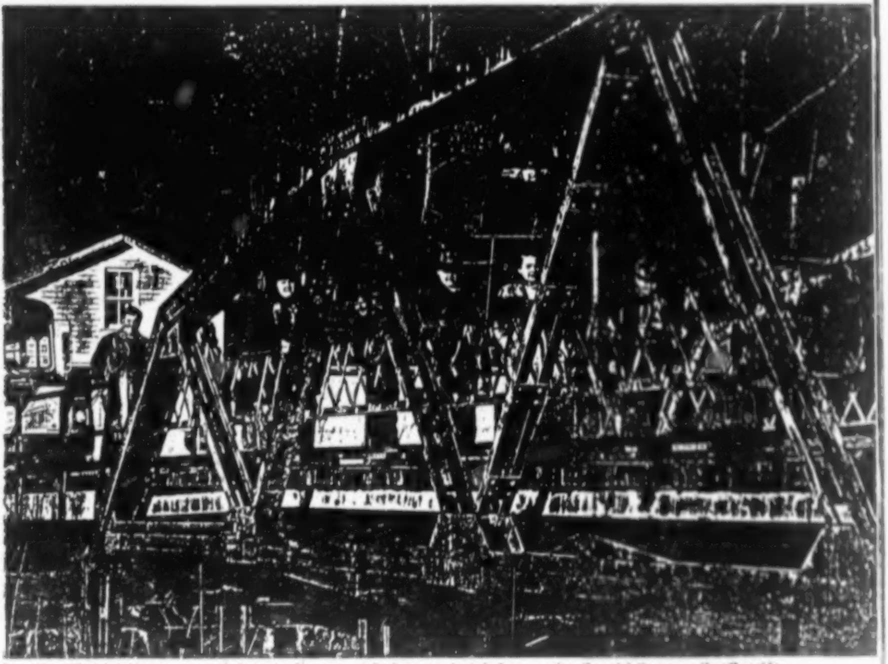
Carrying the banner of economic development, cities are in hot competition for new businesses. Says Heywood Sanders, a professor of urban studies at Trinity University in San Antonio: "Local governments are getting more fiscally crass. They will spend money to attract business and industry instead of taking care of the people and neighborhoods already there."

REPORT CARD ON THE NATION'S PUBLIC WORKS

CATEGORY	GRADE	STRENGTHS	WEAKNESSES
Highways	C+	Federal and state gas tax increases have provided new capital for expansion and maintenance. Pavement conditions are improving.	Congestion is getting worse in high-growth urban and suburban areas. Many aging roads and bridges, particularly in rural areas, need major work.
Mass transit	C−	Federal grants have helped upgrade quality of service in some areas.	The number of transit vehicles is growing twice as fast as ridership. People still prefer driving cars to riding buses and trains.
Aviation	B−	So far regulators and the airline industry have handled increase in demand effectively. Air traffic control system is undergoing a $16 billion modernization.	Airport and airspace congestion is increasing because of strong traffic growth.
Water supply	B−	Locally operated programs assure supply in most areas. The 1986 Safe Drinking Water Act created strict new standards.	In many places, water is priced below costs. Supply is limited in some parts of the West and several cities on the East Coast.
Solid waste	C−	Tougher environmental standards require more rigorous monitoring of solid-waste facilities. Waste-to-energy techniques are gaining as an alternative to landfills.	The cost of safe-disposal facilities is rising fast. Little progress has been made in reducing waste through recycling. People fight new disposal sites where they live.
Hazardous waste	D	Since 1986, government spending on hazardous waste cleanup has risen 500%.	Only a fraction of the two tons of dangerous waste per capita that Americans generate each year is being treated safely. There is a huge backlog of cleanup projects.

What needs fixing? Many of the sewers, bridges, and water systems in America's older cities, built around the turn of the century, are now in disrepair. The Federal Highway Administration's latest report classifies 23% of the 575,600 bridges in the U.S. as structurally deficient: They are either closed or restricted to light traffic. But age does not always imply decay. The pavement on much of the country's four million miles of highways has been improving since 1982, when Congress raised the federal gas tax by a nickel a gallon.

Still, travelers feel that the roads and airports they use are overwhelmed by congestion. According to the Federal Highway Administration, 65% of the traffic at peak travel times on interstates in urban areas moves at an average speed of less than 35 miles an hour, up from 54% in 1983. Though the U.S. has 16,300 public airports—more than the rest of the world combined—no new commercial airports have been built since 1974 (Dallas–Fort Worth). Since then the number of passengers carried has more than doubled to 479 million a year. By 1993 up to one-half of the country's landfills, which collect 95% of the 450,000 tons of garbage Americans generate each day, will fill up and be closed. Partly in an effort to promote alternatives, such as recycling and incineration, cities in some parts of the U.S.



Some West Virginia bridges are so weak that school buses must discharge students before crossing, then pick them up on the other side.

ire doubling and tripling the price of garbage disposal. Says Thomas Whalen, the nayor of Albany, New York: "We will robably have to spend as much on garbage is on the war on drugs."

In its final report to Congress last year, he National Council on Public Works Improvement, which was created in 1984 to ssess the state of America's public works see report card), concluded, "While America's infrastructure is not in ruins, it is inadquate to sustain future economic growth."

America has to face its needs even as the ederal government is moving out of the inrastructure business. Its last heroic public vorks project, the interstate highway sysem, will be complete in 1992. Preoccupied with an unyielding budget deficit, Uncle Sam is doling out less and less money for infrastructure. Heywood Sanders estimates that of the $40.5 billion spent to build and expand highways, airports, sewers, mass transit, and waterworks last year, 46% came from federal grants, down from 54% in 1985. State and municipal governments are stuck with the rest. To get the most for their money, local politicians have come up with four infrastretching strategies:

■ **Infrastretcher No. 1: Make the most of what you've got.** No infrastructure investment generates a greater return than timely maintenance. A study last year by the New York City Department of Transportation for Mayor Edward I. Koch concluded that it is one-third as expensive to maintain a bridge—just cleaning and painting it—as it is to let it deteriorate and then reconstruct it. In his report to Koch, New York City transportation commissioner Ross Sandler pointed out, "Currently, New York City bridges receive virtually no preventive maintenance." As a result, the city must embark on a ten-year, $3 billion program to reconstruct 371 of its 846 bridges. The 80-year-old Manhattan Bridge, which daily carries 78,000 vehicles across the East River, will undergo a $170 million face lift.

Why have cities let upkeep slide? Because politicians make voters happier by

REPORTER ASSOCIATE Rosalind Klein Berlin

HOTOGRAPH BY NINA BARNETT

At Los Angeles's underground control center, engineers monitor data from road sensors that measure traffic flow. By changing the timing of signal lights, they keep cars moving.

sacrificing dull efficiency and putting money someplace else—in schools, parks, and hospitals. As Louisville, Kentucky, Mayor Jerry Abramson says, "It's hard to run for reelection on the theme of 'I kept your sewers from falling apart.'"

To save political hides, localities are creating more public authorities. These independent bodies, made up of appointed officials, can raise money specifically for bridge and sewer maintenance instead of competing for general funds with schools and hospitals. The Port Authority of New York and New Jersey and the Triborough Bridge and Tunnel Authority use the money they collect in tolls to maintain the 11 bridges and four tunnels they operate. As of 1986, the last time a survey was published, all the bridges were classified in good or very good condition. By contrast, 46% of the 846 city-run bridges were found to be in poor or fair condition.

Three years ago the Massachusetts legislature created the Water Resources Authority to repair and replace Boston's ancient sewer system, which has done as much damage to Boston Harbor as Boston Harbor did to Michael Dukakis's presidential campaign. This group can set water rates and, according to executive director Paul Levy, will probably become the largest issuer of revenue bonds in the country. Says Levy: "The average household water and sewer bill is going to have to increase by $50 to $60 per year for the next ten years. The legislators couldn't have taken the heat. They'd get thrown out of office."

One of the trendiest techniques for making the most of existing highways is called incident management. It turns out that 60% of all traffic delays are caused not by lack of capacity but by truck and automobile accidents, from fender benders to jackknifed tractor-trailers. Since these tie-ups often recur near the same locations, why not get the tow trucks to the scene *before* the accident? In Chicago, a huge mobile crane dubbed Mad Max moves disabled trucks off the road in half the time it used to take emergency vehicles to get there.

■ **Infrastretcher No. 2: Reduce demand.** In a society that has grown accustomed to having more where that came from, people pay scant attention to pleas to drive less, fly less, and stop throwing out all those returnable bottles and cans. Going back to Economics 101, the best way to bring demand into sync with supply is through efficient pricing. Airports, which expect a 72% increase in passenger volume by the year 2000, are leading the way. One of the pioneers is Logan in Boston, New England's major air traffic hub. Officials there discovered that general aviation and commuter planes accounted for 40% of takeoffs and landings but only 6% of passengers. This inefficiency was due partly to a landing-fee system based on airplane weight: 747s paid $740 to land, Piper Apaches only $25. To encourage general aviation to use smaller airports and commuter lines to use larger planes, Logan last July instituted a fee schedule based on fixed airport costs, such as navigational aids, as well as weight.

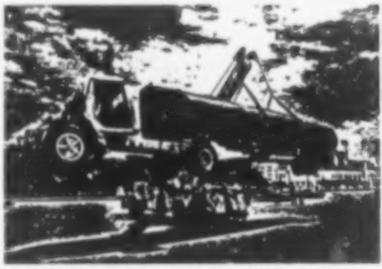
During the last three months of the year, Logan's passenger load was up 3.3%, compared with the same period a year earlier, while the number of takeoffs and landings dropped 7%. In terms of on-time takeoffs, Logan rose from No. 24 to No. 2 among the country's 27 busiest airports. But the new fees were short lived. The U.S. Department of Transportation declared the plan to be discriminatory, and Congress, under pressure from the commuter lines and private plane owners, forced Logan to revert to its old fee schedule by threatening to withhold maintenance funds. Richard Giesser, chairman of the Massachusetts Port Authority, which runs Logan, is appealing the decision. "We're getting blocked when we try to manage better."

More efficient pricing can be applied to highways as well. Only 35% of the two trillion vehicle miles that Americans traveled in 1988 were work related; most trips were made for personal reasons. Congestion pricing—charging drivers more to use the highways during rush hour—would inspire Gramps to leave the bowling alley and head home before 5 P.M.

The hitch is that congestion pricing requires collecting tolls, and that can create even more congestion. At the San Diego–Coronado Bridge, the California Department of Transportation is experimenting with automatic toll collectors, which electronically read tags attached to car windows, and then bill the drivers. According to Michael Shelton, director of the bridge project for the California Department of Transportation, the electronic toll collectors can record fares for cars traveling up to 75 miles per hour. During tests, these drivers didn't slow down, let alone stop.

One of the most effective ways to reduce highway congestion is the good old car pool, now getting renewed attention. According to a study by Jeffrey Lindley, a researcher at the Federal Highway Administration, if one lone commuter of every five jumped into a pool or took mass transit, traffic would decrease roughly 18% during peak hours. The trouble is, car pooling can be inconvenient and is a tough sell: The average occupancy of private commuter vehicles during rush hour today is only 1.3 persons.

One thing that might encourage a solo driver to bring along a friend is the high-occupancy-vehicle (HOV) lane, a corridor reserved for cars carrying more than one person. Introduced in the late Sixties, HOV lanes are proliferating almost as fast as car phones. On Shirley Highway between Springfield, Virginia, and Washington, D.C., cars in two HOV lanes carry 54% more passengers than the other four lanes combined. Houston now has HOV lanes on four of its six major highways and plans to open another 35 miles of HOV lanes by the summer of 1992. According to Paul Bay, assistant general manager of Houston's Metropolitan Transit Authority, riders in the city's HOV lanes save about one minute per mile traveled.



When Chicago's traffic stops flowing, Mad Max gets going. Mobile crane Max, practicing here, can lift 60-ton trucks.

■ Infrastretcher No. 3: Use advanced technology. With seven million cars now registered in the Los Angeles area, driving around the City of Angels is not exactly heaven. By 2010, the Los Angeles metropolitan region is expected to grow by another five million people, to 18.5 million. One eye-popping proposal to fight gridlock: double-decking the Los Angeles freeway. But that would cost up to $50 billion and take 30 years.

No less visionary, but a lot less expensive, is the Automated Traffic Surveillance and Control Center, which monitors traffic primarily in downtown Los Angeles. In a room five floors below ground, at the end of a long labyrinth broken up by several four-inch-thick steel doors, traffic engineers attack congestion as if they were in, as transportation chief Ed Rowe says, "a battle situation." Sensors in the roads feed information on traffic flow to central computers, which regulate traffic signals accordingly. Flashing red lights on three computer screens alert the engineers to unusual traffic patterns, enabling them to dispatch highway patrol and emergency equipment to the scene immediately.

This high-tech attack on gridlock has been hitting the mark. By flushing out the streets through better signal timing and electronic surveillance during the 1984 Olympics, the first major test of the system, Rowe's traffic team increased average travel speeds 15%, and cars consumed 12.5% less fuel than usual. Los Angeles is now planning to install the system citywide, at a cost of roughly $200 million.

To clear disabled vehicles and reduce congestion, Chicago's Minute Men service patrol roams the highways on the lookout for stranded motorists, like this young family.

■ Infrastretcher No. 4: Make dollars go further through innovative financing. In spite of gains from better management and modern technology, city and state infrastructure budgets still fall far short of projected needs. Southern California, for instance, estimated last year that it would cost $110 billion over 20 years to build a freeway and transit system that would enable its citizens to move from place to place as easily as they did in 1984. By incorporating better management and state-of-the-art technology into the plan, transportation officials pared the number to $50 billion—still almost twice as much as the region's share of state transportation revenues through the year 2010. With the federal government easing out of the picture, the money to bridge the gap is coming from individual users and businesses.

The largest potential source is the gas tax. In California, legislators are pushing for an increase in the state gas tax of up to 10 cents per gallon, to 19 cents. An increase is long overdue: For all its griping about congestion, California has the fifth-lowest state motor fuel tax in the U.S. and ranks 48th in per capita spending on transportation.

Throughout the country, the average state gas tax rate has nearly doubled, to 15 cents a gallon, since 1980. This rise has been offset, however, by inflation and increased fuel efficiency. Says Tom Deen, executive director of the Transportation Re-

Commuters to and from Boston's Logan Airport swap salty air for salty language by taking the harbor shuttle instead of driving through the usually jam-packed Callahan Tunnel.

search Board: "We have a ludicrous situation in this country where we spend $650 billion a year to buy and operate our cars and trucks and only $66 billion on the road system." The Federal Highway Administration estimates that by increasing fuel taxes, sales taxes on vehicles, and registration fees, states could raise an additional $23.8 billion per year.

Cities could also take greater advantage of user fees—if the states would let them. Local governments now pay half the $100 billion the nation spends annually to build, operate, and maintain its public works. Yet they are severely hampered when it comes to raising local taxes. A number of states—31 in 1985—impose limits on how much local governments can increase property taxes, and six states restrict the total revenues that local governments can collect annually from any source. Due to such constraints, locally levied user fees account for less than 10% of local highway spending.

To complicate the matter, Washington policymakers are talking about raising the 9 cents a gallon that the federal government collects at the gasoline pump as a way of reducing the budget deficit. State and local governments view this as a huge threat, since a higher federal gas tax would make it much harder for them to raise their own motor fuel taxes. Says Georgia Governor Joe Frank Harris, who has been trying, unsuccessfully, to persuade his legislature to increase the state gas tax 6 cents: "The federal government has to be very careful that what they are doing to reduce the deficit doesn't hurt our efforts. If they aren't going to give money to us, they at least need to give us the ability to raise our own."

A new way to hit the private sector for more money is the so-called special assessment district, a small section of the city that has power to levy taxes and user fees. To expand Route 28, a busy two-lane highway in Fairfax County, Virginia, the state and county created a special taxing district that local politicians think will serve as a model for other communities. Commercial developers along the route pay a surcharge on top of the property tax: an additional 20 cents per $100 valuation. The extra revenue will pay 80% of the $180 million needed to turn Route 28 into a six-lane highway. The payback to landowners? Property values rise.

Another way to tap business is through "proffers," or private-sector donations. To speed up a $200 million expansion of the Louisville, Kentucky, airport, for instance, local businesses recently handed over $380,000 to pay for the required environmental analysis. Waiting for funds from the FAA could have delayed the project a year. In Westboro, Massachusetts, Data General and three other companies invested $350,000 to design an exit ramp, lights, and new lanes to handle congestion on nearby Route 9. But most of the proposed project remains unbuilt, due partly to lack of state funds. Says Brad Stroup, director of public affairs for Data General: "The infrastructure problem has forced industry into confrontation and cooperation with the locals. We are the only ones with deep pockets."

Communities that really want to cut costs should consider privatization. In a survey of 1,086 city and county officials conducted in 1987 by the accounting firm Touche Ross, 45% of the governments that tried to reduce capital costs by using outside suppliers to build and operate public facilities reported savings of 20% or more. Nearly 80% of the respondents reported that privatization will represent a primary means of providing local infrastructure and other government services in the next decade.

When a group of investors realized that a four-year-old state toll road connecting Dulles Airport to Washington, D.C., is accumulating excess cash at the rate of $6 million a year, they decided to explore privatization. They formed the Toll Road Corp. of Virginia after the state legislature legalized the operation of private toll roads last July. Their plan, which needs separate state approval, is to build, own, and operate a toll road between Dulles Airport and Leesburg, Virginia. "This is the premier privatization project for infrastructure in the country, and it's a model," says Ralph Stanley, the former director of the Federal Urban Mass Transportation Administration who heads the group. "If we're successful, we want to do other projects, like wastewater treatment and toll bridges."

What's left to do to make sure public works are efficiently run and well maintained? Plenty. Companies can help reduce highway demand by providing flexible work hours for employees so they can avoid rush hour, by providing buses to train stations to encourage mass transit, and by arranging car pools or giving poolers special parking spaces. But more important, businesses can pressure politicians to manage infrastructure better. Says Dick Giesser of the Massachusetts Port Authority: "Management is the issue." And who understands the rigors and rewards of management better than business?